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February 27, 2017

FILED VIA DELAFILE
Donna Nickerson, Secretary
Delaware Public Service Commission
Cannon Building, Suite 100
861 Silver Lake Boulevard
Dover, DE 19904

Re: Docket No. 16-0649 - Motion by Delmarva Power & Light Company to Convert Evidentiary Hearing

Dear Secretary Nickerson:

Enclosed for filing is Delmarva Power & Light Company's ("Delmarva") Motion to Convert Evidentiary Hearing in the above referenced docket. Delmarva is filing two (2) versions of this Motion, a Public Version and a Confidential Version. This is the Public Version of the Motion.

Should you have any questions or require any additional information, please do not hesitate to contact me.

Very truly yours,

Pamela J. Scott

Enclosures
cc: Senior Hearing Examiner Mark Lawrence
Service List Docket 16-0649

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF DELMARVA POWER & LIGHT COMPANY FOR AN INCREASE IN ELECTRIC BASE RATES AND MISCELLANEOUS TARIFF CHANGES (Filed May 17, 2016)	* * * * *	PSC Docket No. 16-0649

MOTION TO CONVERT EVIDENTIARY HEARING

Delmarva Power and Light Company ("Delmarva"), the Division of the Public Advocate ("DPA") and the Delaware Energy Users' Group ("DEUG") (together, the "Settling Parties"), by and through their undersigned counsel hereby request that the Hearing Examiner convert the evidentiary hearing scheduled for March 7 through March 9, 2017 into a hearing to consider the Proposed Settlement (the "Proposed Settlement") (the executed term sheet reflecting this agreement is attached hereto as "Exhibit A") among the Settling Parties, and state the following in support thereof:

1. On May 17, 2016, Delmarva filed its Application for an Increase in Electric Distribution Base Rates ("Application"), seeking approval of a proposed increase of $62,766,280 in electric base rates, equating to an increase in total revenue of 10.6%. DEUG moved to intervene in these proceedings by petition dated July 5, 2016, which the Commission granted by Order dated July 14, 2016. The DPA intervened in the proceedings, pursuant to 29 *Del. C.* § 8716, on July 8, 2016.

2. On July 28, 2016, the Hearing Examiner issued the Procedural Schedule, setting March 7, 2017 to March 9, 2017 as the dates for the evidentiary hearings on Delmarva's

Application. Since that time, the Settling Parties have reached agreement concerning the Application, and wish to resolve these proceedings by the Proposed Settlement. In view thereof, the Settling Parties request that the Hearing Examiner convert the evidentiary hearings into a hearing to consider the Proposed Settlement. (A finalized and executed Settlement Agreement, the terms which will be consistent with those contained in Exhibit A, will be provided to the Hearing Examiner and Commission Staff later this week.)

3. Delaware statutory law charges the Commission to "encourage" settlements. 26 *Del. C.* § 512(a) ("Insofar as practicable, the Commission shall encourage the resolution of matters brought before it through the use of...settlements"). Delaware law further provides that approval of settlements by the Commission shall be "upon [a] hearing," as requested by this motion. *Id.* §512(c). Modification of procedural schedules to accommodate such settlement hearings has also been granted by this Commission, including in prior Delmarva rate cases. *See, e.g., In re Delmarva Power & Light Co.,* 2005 WL 3617552 (Del. P.S.C. Oct. 11, 2005).

4. Although the Commission Staff has not signed on to the Proposed Settlement, the statute directs the Commission to decide whether to approve a settlement based solely on whether the settlement is "in the public interest." 26 *Del. C.* § 512(c). The statute expressly permits the approval of settlements "whether or not such stipulations or settlements are agreed to or approved by all parties." *Id.*; *see also Constellation New Energy, Inc., v. Pub. Serv. Comm'n,* 825 A.2d 872, 874 (Del. Super. Ct. 2003) (the "statute authorizes the Commission to approve settlements, even ones contested by non-settling parties..."). The Commission has repeatedly relied upon this statutory grant to approve settlements over objections by non-settling parties, *In re Delaware Elec. Cooperative, Inc.,* 2000 WL 36573868 at ¶ 73 (Del. P.S.C. Apr. 25,

2000) ("Moreover, the Commission is authorized to approve settlements if they are in the public interest (even if all parties are not in agreement)"), including in at least two Delmarva rate cases. *See In re Delmarva Power & Light Co.*, 2002 WL 1306032 (Del. P.S.C. Apr. 16, 2002) (settlement approved over objection of intervenor AES New Energy, Inc.); *In re Delmarva Power & Light Co.*, 2012 WL 7149411 (Del. P.S.C. Dec. 18, 2012) (settlement approved over objection of intervenor State Representative John Kowalko).

5. The DPA's approval of a settlement is highly persuasive on the issue of whether the settlement is in the "public interest" because the DPA is charged by statute with the protection of Delaware ratepayers. *Constellation,* 825 A.2d at 883 ("The Court notes that it puts significant weight on the opinion of the Public Advocate, a party charged by statute to protect the Delaware ratepayers, that the settlement is in Delaware's best interest").

6. The only logical and efficient path forward is for the Hearing Examiner to convene a hearing to receive evidence on whether the Proposed Settlement is in the public interest, where the Settling Parties can provide evidence in support of the Proposed Settlement and Staff, to the extent it opposes the Proposed Settlement, can present evidence supporting its own position and can cross-examine the witnesses offered by the Settling Parties. This was the procedure used in the *Constellation* case. *Id.* at 876. Forcing the Settling Parties to proceed with a full evidentiary hearing on the original Application would be inconsistent with both 26 *Del. C.* § 512 and clear Delaware appellate court precedent. *Constellation,* 825 A.2d at 881-882 (Court specifically interprets 26 *Del. C.* § 512 to mean that when a non-unanimous settlement has been reached in a Commission proceeding that establishes rates, a full hearing on all the evidence in the case is not required to review and approve the settlement). Parties settle litigation to avoid incurring additional costs and to avoid the risk associated with an adversarial hearing. *See In re*

Delmarva Power & Light Co., 2000 WL 1035896 at p. 9, ¶g (Del. P.S.C. Jun. 20, 2000) ("settlement. . . reduce[s] the expense of fully litigating the issues").

7. Furthermore, it would make no sense to force DPA and Delmarva to face off in an adversarial hearing immediately after reaching a compromise of their differences on Delmarva's Application. Forcing parties to go to an adversarial hearing after settling their differences would substantially reduce the incentive for parties to settle, which would negate the directive of Section 512 to "encourage the resolution of matters...through the use of...settlements." *See, Constellation,* 825 A.2d at 881-882 ("the legislature has determined that settlements are to be encouraged and that the Commission may approve any settlement it finds to be in the public interest, regardless of whether that settlement has been agreed to by all parties...").

8. The evidence presented at the hearing on the Proposed Settlement should be limited to entry of the pre-filed testimony and exhibits into the record, and testimony on the issue of whether the Proposed Settlement is in the public interest. As noted previously, Staff is free to cross-examine the witnesses that the Settling Parties proffer to testify that the Proposed Settlement is in the public interest, and to proffer its own witnesses to testify about why it believes the Proposed Settlement is not in the public interest. The efficiency and organization of the settlement hearing would be improved by a supplemental pre-hearing conference to address any unresolved issues related to holding a settlement hearing, instead of an adversarial hearing on the merits of the Application.

WHEREFORE, the Settling Parties respectfully request that the Hearing Examiner enter an Order in the form attached as Exhibit B converting the evidentiary hearings

scheduled for March 7, 8 and 9, 2017 into a hearing to determine whether the Proposed Settlement is in the public interest.

Respectfully submitted,

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February 27, 2017
10837367

Exhibit A

Exhibit B

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF DELMARVA POWER & LIGHT COMPANY FOR AN INCREASE IN ELECTRIC BASE RATES AND MISCELLANEOUS TARIFF CHANGES (Filed May 17, 2016)	* * * * *	PSC Docket No. 16-0649

ORDER

Delmarva Power and Light Company ("Delmarva"), the Delaware Public Advocate ("DPA") and the Delaware Energy Users' Group ("DEUG") (together, the "Settling Parties") having moved in the above-captioned docket to convert the evidentiary hearings scheduled for March 7, 2017 through March 9, 2017 to a hearing to consider whether the Proposed Settlement entered into by the Settling Parties is in the public interest, and the Hearing Examiner having found good cause therefor:

IT IS HEREBY ORDERED this _____ day of _____, 2017 that:

1. The adversarial evidentiary hearings scheduled for March 7, 2017 through March 9, 2017 are cancelled;

2. A hearing to consider whether the Proposed Settlement is in the public interest shall be held starting at 10:00 a.m. on March 7, 2017, at which time the parties to this docket shall present evidence as to whether the Proposed Settlement is in the public interest; and

3. A supplemental pre-hearing teleconference shall be held on _____, 2017 at ____ a.m./p.m., which shall be attended by all the parties to this docket.

_____
Senior Hearing Examiner

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF DELMARVA POWER & LIGHT COMPANY FOR AN INCREASE IN ELECTRIC BASE RATES AND MISCELLANEOUS TARIFF CHANGES (Filed May 17, 2016)	* * * * *	PSC Docket No. 16-0649

COMPENDIUM OF AUTHORITIES CITED TO IN THE
SETTLING PARTIES MOTION TO CONVERT EVIDENTIARY HEARING

Dated: February 27, 2017

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TABLE OF AUTHORITIES

TAB 1

2005 WL 3617552 (Del.P.S.C.), 245 P.U.R.4th 466

Re Delmarva Power and Light Company

PSC Docket No. 04-391
Findings, Opinion, and Order No. 6746

Delaware Public Service Commission

October 11, 2005

APPEARANCES: On behalf of Delmarva Power & Light Company: RANDALL V. GRIFFIN, ESQUIRE. On behalf of the Division of the Public Advocate: G. ARTHUR PADMORE, ESQUIRE. On behalf of the Delaware Public Service Commission Staff: JAMES MCC. GEDDES, ESQUIRE, ASHBY & GEDDES, Rate Counsel and BRUCE H. BURCAT, Executive Director, CONNIE S. MCDOWELL, Chief of Technical Services, KAREN L. NICKERSON, Secretary, JANIS L. DILLARD, Regulatory Policy Administrator, Delaware Public Service Commission Staff. On behalf of Conectiv Energy Supply, Inc.: I. DAVID ROSENSTEIN, ESQUIRE. On behalf of the Delaware Energy Users Group: BRIAN R. GREENE, ESQUIRE, CHRISTIAN BARTON LLP. On behalf of the Retail Energy Supply Association, Select Energy, Inc. and Strategic Energy LLC: DANIEL CLEARFIELD, ESQUIRE, WOLF, BLOCK, SCHORR & SOLIS-COHEN LLP. On behalf of Premcor Refining Group: KENNETH G. HURWITZ, ESQUIRE, HAYNES & BOONE.

Before McRae, chair, and Lester, Conaway, and Winslow, commissioners

BY THE COMMISSION:

BACKGROUND

1. The Electric Utility Restructuring Act of 1999 (the 'Act') required Delmarva Power & Light Company ('Delmarva' or 'the Company') to file a restructuring plan under which it would provide standard offer service ('SOS') for an initial transition period ending on September 30, 2002 for non-residential customers and on September 30, 2003 for residential customers. The restructuring plan and related matters relevant to customer choice and restructuring were approved in a series of Orders issued in Docket No. 99-163. Among other things, the approved restructuring plan reduced rates for residential customers and froze those reduced residential rates and the applicable rates for non-residential customers until the end of the respective transition periods.

2. Prior to the end of the initial transition periods, a merger involving Delmarva and Potomac Electric Power Company was proposed. In the resolution of that docket, the Delaware Public Service Commission (the 'Commission') approved a settlement that authorized the proposed merger on the condition that Delmarva's obligation to provide SOS would continue until May 1, 2006 at rates that were reset to reflect market prices at that time. (Docket No. 01-194).

3. On October 19, 2004, noting that SOS rates had increased significantly in other jurisdictions once the freeze on supply rates had been lifted, the Commission initiated this docket to 'explore issues related to the selection of an SOS supplier for [Delmarva's] service territory and the appropriate prices to be charged for SOS after that date.' (Order No. 6490, Oct. 19, 2004 at £ 3). In Order No. 6490, the Commission discussed certain statutory requirements and prior cases involving the provision of SOS to Delmarva customers pursuant to the Act. The Order established a process pursuant to which major policy issues would be resolved in an initial phase of the docket, while other technical and policy issues would be reserved for resolution in one or more subsequent phases of the docket. The Commission established February 28, 2005 as the deadline for the conclusion of the first stage and appointed Senior Hearing Examiner William F. O'Brien as a monitor to oversee the proceedings.

4. Pursuant to the Commission's instructions in Order No. 6490, Staff conducted two workshops, during which it solicited both written and oral comments from the participants. On January 5, 2005, Staff submitted a position paper addressing several issues that the parties agreed were fundamental SOS issues.

5. On March 22, 2005, in Order No. 6598, the Commission reviewed the report and recommendations prepared by Staff that had been the subject of written comments and oral argument presented by parties that had participated in the docket. In Order No. 6598, the Commission adopted all of Staff's recommendations notwithstanding opposition from certain parties. First, the Commission determined that SOS in Delaware would be provided pursuant to a 'wholesale' model, whereby the Commission would select the incumbent distribution utility (Delmarva) as the SOS provider. Delmarva would secure the power to serve SOS customers from the wholesale power market but would continue to interface directly with the customer. This model was selected over various forms of the 'retail' model, whereby the Commission would select one or more SOS providers through some form of competitive bidding process and those providers would assume some or all of the duties of interfacing with the retail SOS customer.

6. Second, the Commission deferred the remaining Phase 1 issues to Phase 2, including the method by which the wholesale power would be procured, the composition of the 'retail adder' or margin that Delmarva would include in its SOS rates, and the use of SOS to promote various societal benefits (such as renewable resource and demand side management programs). The Commission again appointed Hearing Examiner O'Brien to monitor the Phase 2 proceedings and to handle any disputes regarding the provision of information.

7. In Phase 2, the parties established a two-track procedural schedule consisting of a litigation track for the determination of the composition of the retail adder and a non-litigation track for the remaining, primarily policy-driven, issues. These latter issues included Commission oversight of the process, splitting of rate classes, and rate translation of bids into tariffs.

8. After Staff had conducted four workshops and had solicited oral and written comments on the issues, Staff, the Division of the Public Advocate (the 'DPA '), the Delaware Energy Users Group ('DEUG'), Delmarva, and Conectiv Energy Supply, Inc. ('CESI') reached a proposed settlement of all of the issues, including the litigation-track retail adder. These parties submitted the proposed settlement to the Hearing Examiner on July 14, 2005. On July 14, 2005, the Hearing Examiner modified the procedural schedule to provide that the signatories to the proposed settlement would submit pre-filed testimony in support of the settlement on July 18, 2005, and that opponents would submit pre-filed testimony in opposition to the settlement on July 26, 2005. A hearing was scheduled for August 1-2, 2005, with post-hearing briefs due on August 16, 2005.

9. Staff witness Janis L. Dillard, Delmarva witness Peter E. Schaub, DPA witness Andrea C. Crane, Conectiv witness Champe Fisher and DEUG witness Dr. Alan Rosenberg all filed testimony supporting the proposed settlement on July 18, 2005. Subsequently, the parties requested additional time to try to reach a unanimous settlement. The testimony filing date was extended from July 26 to July 29, and the evidentiary hearing originally scheduled for August 1 and 2 was postponed to August 4.

10. The parties were unable to reach a unanimous settlement, and, therefore, on July 29, 2005, Select Energy, Inc. ('Select') submitted the pre-filed testimony of witnesses Leonard Navitsky and Marc Hanks in opposition to the proposed settlement. The Premcor Refining Group ('Premcor') submitted a letter from Michael Polluf, Refinery Manager, opposing the proposed settlement.

11. On August 1, 2005, Senior Hearing Examiner O'Brien conducted the public comment portion of the hearing. Only one non-party attended the public comment session, and, although this person asked several questions, she offered no public comment.

12. On August 4, 2005, the Hearing Examiner presided over a duly-noticed evidentiary hearing at which the Settling Parties presented the proposed settlement agreement and offered testimony in support of the settlement. The Hearing Examiner also heard oral surrebuttal testimony by the settlement proponents. Select's

witnesses presented their pre-filed testimony. Moreover, although the Retail Energy Supply Association ('RESA') had not submitted any testimony in opposition to the proposed settlement, its counsel appeared at the evidentiary hearing and cross-examined the settlement proponents' witnesses. At the conclusion of the hearing, the record, consisting of 10 exhibits and a 676-page transcript of the hearing, was closed.

13. On August 16, 2005, the parties submitted their post-hearing briefs in favor of or in opposition to the proposed settlement.

14. On September 1, 2005, Senior Hearing Examiner O'Brien issued his findings and recommendations, in which he found the proposed settlement to be in the public interest and recommended that the Commission approve it.

15. On September 13, 2005, RESA, Select, and Strategic submitted a combined set of exceptions to the Hearing Examiner's findings and recommendations. Also, on September 13, 2005, Premcor submitted a letter to the Commission stating its opposition to the Hearing Examiner's findings and recommendations. DEUG filed in support of the Hearing Examiner's findings and recommendations. Commission Staff, DPA, and Delmarva submitted letters stating that they took no exceptions.

16. On September 20, 2005, the Commission met at its regularly-scheduled public meeting to consider and deliberate on the Hearing Examiner's proposed Findings and Recommendations. At that meeting, we adopted the Findings and Recommendations of the Hearing Examiner and approved the Settlement Agreement into which the Settling Parties had entered.

17. On October 5, 2005, the parties executing the Settlement Agreement and Premcor filed an amendment to the Settlement Agreement, which amendment provides an alternative mechanism for assigning certain billing system costs to Premcor and other customers. The amendment was unopposed and, at the Commission's October 11, 2005 meeting, was discussed and approved.

18. We set forth herein the reasoning behind our adoption of the Hearing Examiner's Findings and Recommendations and our approval of the Settlement Agreement, as amended.

THE SETTLEMENT

*1 19. The proposed settlement provides that Delmarva will provide SOS to all customer classes, with no specified termination date. There will be two categories of SOS: (1) a fixed price SOS available to all but the largest customers (the GS-T customers); and (2) an Hourly Priced Service ('HPS') that is mandatory for GS-T customers and will be offered as an option for GS-P customers. In order to take HPS, a GS-P customer must make an affirmative election prior to the Request for Proposal ('RFP') process, and must have an interval meter or be willing to pay for installation of such a meter prior to beginning HPS. GS-P customers will have the opportunity to elect HPS or fixed price SOS every year. [1]

20. A competitive RFP process will be used to procure the full requirements of customers eligible for a fixed price SOS. Bidders will be asked to bid seasonally, but the retail rates will be developed using the bids and converting them into the existing rate design structures. In consultation with the other parties in this docket, Delmarva is in the process of developing a Full Requirements Service Agreement ('FSA') and an RFP (collectively, a 'Bid Plan'). The proposed settlement calls for a consultant selected by the Commission to monitor and participate in the bidding process. The Company will pay for the consultant, with the expenses being recovered in charges that are part of the fixed price SOS. That consultant, as well as the DPA and its consultant, will be permitted unfettered access to the bid process, subject to confidentiality concerns.

21. To provide rate stability for residential and small commercial customers, Delmarva will initially procure 1/3 of the load with a three-year contract (which will actually be 37 months for the first three-year contract), 1/3 with a two-year contract (which will actually be 25 months for the first two-year contract),

and 1/3 with a one-year contract (which will actually be 13 months for the first one-year contract).[2] By the end of the second year, there will be a portfolio of three-year contracts to serve this load, and each year thereafter, a new three-year contract for 1/3 of that load will be entered into to replace the expiring one. One-year contracts will be used for all other customer classes eligible for the fixed price SOS.

22. There are two major components of the SOS retail supply rates. First is the Full Requirements Costs ('FRC'), which, with the exception of the Volumetric Risk Mechanism ('VRM'),[3] is comprised of the costs that Delmarva pays to the winning bidders. Absent a Commission finding of exceptional circumstances, the FRC component will be reset and fixed for 12 months. The FRC will be trued up annually, and this will result in the retail rate for SOS being reset on an annual basis.

23. The reasonable allowance for retail margin ('RARM') mandated by the Act is comprised of several elements: (1) incremental expenses incurred (a) to provide fixed price SOS and HPS; (b) to administer the VRM applicable with respect to fixed price SOS customer load; and (c) carrying costs on Cash Working Capital for fixed price SOS and HPS; (2) $2.75 million per 12-month period, which for the Year 1 and Year 2 rates, is deemed to include any carrying costs on incremental capitalized costs associated with providing fixed price SOS and the VRM, but does not include the separately-calculated carrying costs for capitalized billing system software costs needed to bill and track HPS costs and revenues and also does not include any return on investment that is removed from distribution rates as supply-related; and (3) for GS-T customers and those in the GS-P class that have elected HPS, the allocable share of the above categories plus an amortized amount, including carrying costs on the unamortized balance of the capitalized billing system software costs and interface costs needed to bill and track HPS costs and expenses.[4] In the event that investment is removed from distribution rates in a future distribution base rate proceeding as supply-related, the RARM shall include an additional component comprised of the rate necessary to recover the same revenue requirement components as would have been applied if such investment were to have remained in distribution rates *e.g.*, depreciation expense, return on investment grossed-up for taxes, etc.). Such an adjustment to the RARM shall be made without regard to any other cost component.

24. Delmarva will establish the incremental costs of providing SOS by conducting a lead-lag study to determine its cash working capital requirements. The calculation of these requirements will use Delmarva's total weighted cost of capital grossed up for income taxes. Delmarva will apply its grossed-up cost of capital to the results of the lead-lag study to determine its cash working capital requirements in mills per kWh for each customer class. It will estimate its other incremental capital costs and expenses and provide the Staff and DPA with the supporting workpapers, documents, cost centers and internal work order numbers that Delmarva uses to collect and track costs. These estimates will be reconciled in a proceeding that will be held after actual cost data are known. After this one-time reconciliation, the RARM will remain fixed unless changed by the Commission.

25. The combination of the costs paid for the capacity and energy plus the RARM is designed to comply with the Act's mandate that the SOS price after the end of the transition periods be 'based upon and/or representative of regional wholesale electric market prices, plus a reasonable allowance for retail margin to be determined by the Commission.' 26 Del. C. § 1006(a)(2) c.

26. The proposed settlement also permits Delmarva to implement a pass-through mechanism pursuant to which its retail transmission rates will be developed and billed on the same basis that PJM and FERC use to develop rates and bill Delmarva for transmission. Currently, Delmarva's Delaware transmission rates are designed so that in the aggregate, they collect what PJM charges Delmarva. However, PJM bills based on peak load capacity and Delmarva's retail rates currently bill based on monthly billing demand for larger customers and on a kWh basis for residential and smaller commercial and industrial customers. The settlement proposal reduces the potential for mismatches between FERC costs and retail rate recovery and provides an incentive for customers to participate in demand response programs.

27. As of May 1, 2006, all residential customers and all commercial, industrial, governmental, and other customers other than GS-T customers and electing GS-P customers will be eligible for fixed price SOS.[5] SOS rates will vary

by customer type because the prices will be based on the winning bids received from wholesale suppliers under an RFP bidding process. The supply requirements for residential and the smallest non-residential customers will be bid out as one group. MGS-S customers will form another group, and their load will be bid for separately. LGS-S customers will form a third group, and non-electing GS-P customers will comprise the fourth group. (Exhs. 2, 3).

*2 *THE HEARING EXAMINER'S PROPOSED FINDINGS AND RECOMMENDATIONS*

1. The Proposed Settlement Complies With the Act.

28. The Hearing Examiner began by observing that the Act provides that if Delmarva is the SOS supplier, the SOS price shall be revised from time to time for each customer rate class to be representative of the regional wholesale electric market price plus a reasonable allowance for retail margin, and that the Commission may review the SOS price to determine whether it continues to reflect the regional wholesale electric market price plus a reasonable allowance for retail margin. 26 Del. C. § 1010(a)(2)(C). (Hearing Examiner's Report and Recommendations at £ 39) (hereafter ('HER at ___'). He found that the proposed settlement satisfied each of those requirements.

29. First, the power to provide SOS would be acquired at a price 'representative of the regional wholesale electric market price' because Delmarva would obtain that power either through PJM's competitive markets (in the case of hourly-priced SOS) or through a competitive bidding process. Moreover, the integrity of the bidding process would be assured by the presence of an outside consultant who would monitor the process and report to the Commission. (HER at £ 40).

30. The Hearing Examiner also found that the proposed settlement contained a 'reasonable allowance for retail margin' as required by the Act. The RARM proposed in the settlement includes Delmarva's incremental cost of providing SOS and a component for return (profit). The RARM further contains a true-up provision to capture costs to the extent they were not identified or recovered in the first year's rates and also has a 'catch-all' provision to capture any other cost category that may have been overlooked. (HER at £ 41).

2. The Proposed Settlement Is In The Public Interest.

31. The Hearing Examiner next concluded that the proposed settlement was in the public interest. First, he found that the proposed settlement was supported by a variety of divergent interests: Staff, which represented the interests of ratepayers and regulated utilities; the DPA, which represented all ratepayers with a primary focus on residential and small commercial customers; DEUG, which represented certain large customers, including members of the GS-T class, which would be the only customers subject to the mandatory HPS form of SOS; CESI, which represented a prospective bidder in the RFP process to supply Delmarva with power; and Delmarva, the SOS provider and local distribution company. (HER at £ 43). He agreed that the public interest argument would be stronger if the retail marketers had joined the agreement, but observed that the retail marketers, who would be competing with Delmarva, had 'a direct interest in making the SOS service as unattractive as possible in order to increase their chances of gaining market share.' (HER at £ 44).

32. The Hearing Examiner further found that the retail marketers' interests had been considered in the negotiation of the proposed settlement. He identified several terms in the proposed settlement that benefit retail marketers: (1) the annual resetting of rates to better reflect current market prices; (2) the elimination of returning customer rules; (3) the addition of the RARM, which includes a profit margin, on top of wholesale prices (to provide 'headroom' under which competitors can price their services); and (4) restructuring how Delmarva charges for transmission and ancillary rates to correspond more closely with how PJM charges retail marketers for such services (to enhance a marketer's ability to match its price components with the SOS pricing). (HER at £ 45).

33. The Hearing Examiner rejected the retail marketers' arguments that the proposed settlement should be modified: (1) to require all large commercial and industrial customers to take HPS SOS; and (2) to increase the RARM

to be more representative of 'actual' costs (which they claimed was better reflected in Delmarva's original pre-settlement position). First, the Hearing Examiner found that imposing mandatory HPS on all large commercial and industrial customers would reduce the choice available to those customers because, if they would be unable to take fixed-price SOS from Delmarva; their only option would be to take a fixed-price service from a retail marketer, which they might not want to do. The Hearing Examiner quoted the DPA to explain why that was inappropriate:

*3 Although Select argues that HPS provides better price signals to customers, Select admitted that it has no Delaware customers taking HPS. It is ironic that Select is promoting implementing HPS in Delaware, even though none of its customers in Delaware take HPS. Clearly, Select does not need [Delmarva] to offer an HPS so that it can be put on a level playing field with [Delmarva] because Select itself has no customers on HPS. Select's proposal to increase mandatory HPS appears to be simply a ploy to drive customers away from SOS. DPA witness Crane explained in her testimony that it would be Select, not Delaware ratepayers, who would benefit under Select's proposal.

(HER at £ 47).

Furthermore, the Hearing Examiner found that even if further restricting the availability of fixed price SOS somehow advanced competition, that was outweighed by the interests of affected customers that may wish to remain on SOS but who seek the stability of a fixed price service. He was persuaded by the testimony of DEUG witness Rosenberg, who observed that some large customers might not find HPS attractive because of the volatility, which would create budgeting chaos and uncertainty. (HER at £ 47).

34. The Hearing Examiner next addressed the retail marketers' argument that there was not substantial evidence on the record to support the RARM. First, he noted that the settlement proponents' witnesses had testified that the RARM components would cover Delmarva's incremental costs and that the proposed return would satisfy the statutory requirement of a 'reasonable' retail margin, and that the expert testimony constituted record evidence. (HER at £ 49). Second, the fact that Delmarva originally supported larger retail margins than those espoused in the proposed settlement did not mean that the profit margins in the proposed settlement were inadequate or otherwise failed to encourage competition. Third, he observed that under Delaware law, the parties contesting a settlement do not have a right to a full trial on their issues; rather, the adjudicator of a contested settlement need only know enough about its merits and the identity of the parties to the settlement to be able to evaluate the settlement. (HER at £ 49, *citing In re Amsted Industries, Inc. Litigation*, 521 A.2d 1104 (Del. Ch. 1986); *Rome v. Archer*, 197 A.2d 49, 53 (Del. 1964)).

35. Next, the Hearing Examiner noted that even if the parties had fully litigated the RARM component of the proposed settlement, their positions would still have been substantially divergent and 'determination of the 'correct' numbers would remain elusive' because the parties' positions would largely depend on their views of cost allocation and risk valuation — a subject on which experts frequently disagree. (HER at £ 50). Avoiding the costs associated with fully litigating this issue alone supported a conclusion that the proposed settlement was in the public interest. (HER at £ 50).

36. Finally, the Hearing Examiner rejected Premcor's objection to the proposed settlement that it should not have to bear any of the cost of a system that it was not using. He noted that Premcor's witness at the evidentiary hearing testified that if Premcor's load serving entity was no longer qualified as such by PJM, it 'would probably have to fall back to Delmarva.' (HER at £ 51, quoting Tr. at 567). As the SOS supplier, Delmarva would be obligated to provide supply to Premcor under HPS service at any time if Premcor requested Delmarva to do so. The costs for which Premcor (and others) would be responsible are the costs of establishing the hourly billing system, and the Hearing Examiner found that those costs would exist whether or not Premcor takes HPS initially or not. (HER at £ 51).

OPINION

*4 37. *Twenty-six Del. C.* § 512 encourages the resolution of matters brought before the Commission through stipulations and settlements. Indeed, Section 512(a) of the Public Utilities Act specifically exhorts us to encourage the parties before it to resolve matters by stipulation or settlement. We may approve such stipulations or settlements, even if all parties do not agree, if we find the resolution contemplated by the stipulation or settlement to be in the public interest. 26 Del. C. § 512(c); *Constellation New Energy, Inc. v. Public Service Commission*, 825 A.2d 872, 882 (Del. Super. 2002) (...the legislature has determined that settlements are to be encouraged and that the Commission may approve any settlement it finds to be in the public interest, regardless of whether that settlement has been agreed to by all the parties.').

38. We have reviewed the record and the Findings and Recommendations of the Hearing Examiner, and we agree with the Hearing Examiner that this settlement is in the public interest. For the reasons set forth by the Hearing Examiner, we find that the settlement complies with the requirements of 26 Del. C. § 1006(a)(2)(c), which provides that if Delmarva is the SOS provider (which it is), then the SOS price must be representative of the wholesale electric market price, plus a 'reasonable allowance for retail margin.' We reject the retail marketers' assertion that expert opinion testimony is not substantial evidence and that this settlement is not supported by substantial evidence; indeed, we believe that the Superior Court rejected a similar argument that Constellation New Energy made in its appeal of our decision in Docket No. 01-194. In Constellation New Energy, Constellation argued that the settlement proponents and the Commission bore the burden of establishing that each aspect of the settlement must be supported by specific numeric analysis. The Superior Court, however, disagreed, stating:

This case involves judicial review for the first time of a statute authorizing settlements of disputes before the Commission. That statute authorizes the Commission to approve settlements, even ones contested by non-settling parties, where the Commission finds such resolution to be in the public interest.

Constellation New Energy, 825 A.2d at 874.

39. Later in the opinion, the Court described Constellation's argument with respect to the settlement's provision for the establishment of the regional wholesale electric market price as follows:

Constellation criticizes the Commission because it did not rely on any quantitative analysis as to market prices. Essentially, it maintains that the Commission did not identify any numerical evidence of the 'regional wholesale market price,' or reasonable allowance for retail margin.' Constellation concludes that since the Court cannot identify — and therefore cannot review — the components of the price determination formula set up under section 1006, the Court cannot find that the Commission's decision was based on substantial evidence.

*5 *Id.* at 884. The Superior Court, however, disagreed:

> However, several parties to the settlement and appellees point out that there is no single 'wholesale price' that can be said to be 'representative.' This is because any such wholesale price is necessarily a composite of the prices of capacity, energy and ancillary service, each of which will vary depending on whether one looks at today's prices, future price curves generated by models, or bid and ask prices in future markets. Additionally, all of these factors are necessarily evaluated by each market participant through the lens of its perceptions of the risks assumed for variations in weather, customer usage, risks of lost or added customers, and other forces. Therefore, they conclude, any determination as to whether a particular standard offer service price is representative of regional wholesale market price plus a reasonable allowance for retail margin necessarily entails judgments not easily reducible to a mathematical formula. That is why, the argument continues, it was necessary for the Commission to take the 'end results' approach, relying on the experts' opinions that the settlement's rates were reasonable approximations.

Id. at 884-85. After reviewing other corollary arguments of Constellation and setting forth the expert testimony upon which the Commission relied, the Court concluded: 'The foregoing constitutes substantial evidence from which the Commission could conclude that approval of the settlement with the proposed rates were in the public interest.'*Id.* at 887.

40. We further observe that in Section 1002 of the Act, the Legislature declared that one of the standards governing the Commission's oversight of the transition process is that 'customers shall have the right to choose among electric suppliers.' 26 Del. C. § 1002 (a)(2).[6] We believe that the retail marketers' proposal to require HPS SOS for all large commercial and industrial customers (defined as all GS-T, GS-P and LGS customers having a PLC of greater than 600 kW) would reduce the right of these customers to choose their electric supplier, as DPA witness Crane testified. *See* Tr. at 497. We do not believe that promotion of retail competition, to the exclusion of all other considerations, is the be-all and end-all of the Act. We must take other considerations into account, and we do not interpret the Act as precluding us from doing so.

41. The Settlement Agreement also results in reduced regulatory expense, which is a benefit to Delmarva customers because it reduces the legal and other rate case expense costs that Delmarva will seek to recover in its next case (which has been filed). In a time of rising costs for nearly every commodity, this cost limitation is certainly in the public interest.

42. We rejected Premcor's objections to the original Settlement Agreement for the reasons set forth by the Hearing Examiner. In particular, we note that Premcor, like other customers, has the right to use a competitive retail supplier or to take a Delmarva-provided SOS. Delmarva has incurred costs, in this instance, billing system costs, to be ready to provide an hourly form of SOS (HPS SOS) to Premcor and other customers within the GS-T customer class and those GS-P customers that elect this form of SOS. Thus, it is reasonable that all such customers pay a share of those 'make ready' costs even if, at any particular moment in time, some or all of those customers may not be using the service. The Settlement Agreement provided one reasonable approach, based on peak load, for assigning these costs among customers that will have the right to take the HPS form of SOS. The amendment to the Settlement Agreement provides a different, but also reasonable, mechanism using a per customer charge, except that peak load is used for 'smaller' customers within this group of generally large customers.

43. For these reasons, as well as those set forth in the Hearing Examiner's Findings and Recommendations, we hereby adopt the Findings and Recommendations of the Hearing Examiner in their entirety. (4-0).

MISCELLANEOUS

*6 44. On September 15, 2005, Delmarva filed two documents developed as part of the process for the solicitation of electric supply to meet its SOS obligations on and after May 1, 2006. The first of these documents consists of a single page identifying the Service Types of the customer groups for which supply will be separately solicited, the approximate loads of each of those groups (the Peak Load Contribution or 'PLC') and the contract duration. The second document is a draft request for proposal ('RFP') that will be sent to prospective bidders. The attachments to the RFP included various forms that bidders would need to complete in order to participate in the process or, upon winning a bid, to complete the contemplated transaction. A draft Full Requirements Supply Agreement ('FSA'), that the winning bidders would be required to sign, is also attached as an appendix to the RFP.

45. Delmarva's September 15, 2005 filing was served on all parties to the proceeding. At the Commission meeting on September 20, 2005, Delmarva requested that the Commission take appropriate steps to solicit any comments that other parties may have on the draft documents and, if possible, to consider approving these documents for use in Delmarva's SOS solicitation at the Commission's meeting on October 11, 2005. The Commission directed Hearing Examiner O'Brien to solicit such comments and Staff has reported back that no such comments have been received. Staff has also indicated that it has reviewed the documents and does not propose any changes to them.

46. Delmarva has requested that the Commission approve the form of these documents, including the FSA with a recognition that minor changes to the documents may be made as the result of continuing discussions with Staff and other parties, or from feedback received in pre-bid meetings with prospective bidders. [7]

ORDER

AND NOW, this 11th day of October, 2005, *IT IS HEREBY ORDERED*:

1. That the Findings and Recommendations of the Hearing Examiner dated September 1, 2005 (attached to the original hereof as Exhibit 'A') recommending that the parties' Settlement Agreement be approved are hereby approved and adopted in their entirety. The September 28th amendment to the Settlement Agreement is also approved (attached to the original hereof as Exhibit 'B').

2. The Commission hereby approves the form of the documents filed on September 15, 2005, and explicitly recognizes that some changes to these documents may be necessary or appropriate as the RFP process proceeds. The Commission will not require that each such change be brought back to the Commission for a further approval, but does direct the Company to ensure that Staff and the Public Advocate are made aware of any such changes. To the extent that Staff or the Public Advocate believe that the changes are significant enough to warrant further Commission consideration, the Commission will review any such request.

3. That the Commission retains the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

EXHIBIT 'A'

REPORT OF THE HEARING EXAMINER

DATED: September 1, 2005

*7 William F. O'Brien, duly appointed Hearing Examiner in Stage 1 and Stage 2 of this docket, pursuant to Commission Orders Nos. 6490 (Oct. 19, 2004) and 6598 (Mar. 22, 2005), reports to the Delaware Public Service Commission ('Commission') as follows:

I. APPEARANCES

On behalf of the Delaware Public Service Commission Staff: JAMES McC. GEDDES, ESQUIRE, ASHBY & GEDDES, Rate Counsel. On behalf of the Division of the Public Advocate: G. ARTHUR PADMORE, ESQUIRE. On behalf of Delmarva Power & Light Company: RANDALL V. GRIFFIN, ESQUIRE. On behalf of Intervenor Conectiv Energy Supply, Inc. I. DAVID ROSENSTEIN, ESQUIRE. On behalf of Intervenor Delaware Energy Users' Group: BRIAN R. GREENE, ESQUIRE, CHRISTIAN & BARTON, LLP. On behalf of Intervenor Retail Energy Supply Association: DANIEL CLEARFIELD, ESQUIRE, WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP. On behalf of Intervenor Select Energy, Inc.: FREDERICK LEE KLEIN, ESQUIRE. On behalf of Intervenor Premcor Refining Group: MR. JAMES T. FUESS.

II. BACKGROUND

1. Delaware's Electric Utility Restructuring Act of 1999 ('Restructuring Act ') established a framework under which Delmarva Power & Light Company ('Delmarva' or 'DP&L') and Delaware Electric Cooperative, Inc. would surrender their exclusive franchises to serve retail electric utility customers, thereby providing competitive retail electric marketers

the opportunity to compete for customers within those utilities' service territories. Under the Restructuring Act, those customers who do not choose an electric supplier will take 'standard offer service' ('SOS') from the 'standard offer service supplier' after the applicable 'transition period.' [8] In this docket, the Commission selects the SOS supplier for Delmarva's service territory and establishes the process under which SOS supply will be procured and priced.

2. The statutory transition period for all customer classes in Delmarva's service territory ended in September 2003. In the early part of 2002, however, as part of the resolution of its merger with PEPCO Holdings, Inc., Delmarva agreed to serve as the SOS supplier for its service territory until May 1, 2006, and to freeze its SOS rates (with certain exceptions) until May 1, 2006. [9] The SOS prices would then be reviewed in connection with a process intended to result in the selection of an SOS supplier for the period beginning May 1, 2006.

3. On October 19, 2004, noting that SOS rates had increased significantly in other jurisdictions once the freeze on supply rates had been lifted in those jurisdictions, the Commission opened this docket to 'explore issues related to the selection of an SOS supplier for DP&L's service territory and the appropriate prices to be charged for SOS after that date.' [10] In that Order, the Commission adopted Staff's proposal to conduct this proceeding in three stages: (1) resolving the larger, fundamental issues underlying the selection of a supplier and the setting of SOS rates; (2) crafting the necessary rules or procedures for implementing the choice of an SOS supplier(s) and establishing SOS rates; and (3) implementing the selection and pricing mechanisms from the second stage to determine the post-May 2006 SOS supplier and SOS rates. In addition, the Commission established a deadline of February 28, 2005 for the conclusion of the first stage and appointed a Hearing Examiner as a monitor to oversee the proceedings.

4. Pursuant to the Commission's directives in Order No. 6490, Staff conducted two workshops, through which it solicited written and oral comments from the participants, and then, on January 5, 2005, submitted a position paper addressing several issues that the parties agreed were fundamental SOS issues. On March 22, 2005, the Commission adopted all of Staff's recommendations, as follows, despite opposition from certain parties. (PSC Order No. 6598.)

5. First, the Commission determined that SOS in Delaware would be provided pursuant to a 'wholesale' model, whereby the Commission would select the incumbent distribution utility (DP&L) as the SOS provider, who would secure the power to serve SOS customers from the wholesale power market but would continue to interface directly with the customer. The 'wholesale' model was chosen over various forms of the 'retail' model, whereby the Commission would select one or more SOS providers through some form of competitive process and those providers would assume some or all of the duties of interfacing with the retail SOS customer. (*Id.*)

6. Second, the Commission decided to defer the remaining Stage 1 issues to Stage 2, including the method by which the wholesale power will be procured, the composition of the 'retail adder' or margin that Delmarva would include in its SOS rates, and the use of SOS to promote various societal benefits (*e.g.*, renewable resources and demand response programs). In addition, the Commission again appointed a Hearing Examiner 'to superintend and monitor the Stage 2 process and to deal with any disputes regarding the adequate provision of relevant information.' (*Id.*)

7. In Stage 2, the parties established a two-track procedural schedule consisting of (1) a litigation track for the determination of the composition of the 'retail adder' and (2) a non-litigation track for the remaining issues, which were considered primarily policy-driven and which could be resolved without evidentiary hearings. Track 2 issues included Commission oversight of the process, splitting of rate classes, and rate translation of bids into tariffs, as well as certain issues that the Commission deferred from Stage 1 to Stage 2.

8. After conducting four workshops and soliciting written and oral comments on the issues, however, certain parties agreed on a 'Proposed Settlement,' dated July 14, 2005, regarding all issues from both tracks. As a result, the Hearing Examiner consolidated the two tracks and, rather than conduct a hearing solely on the 'retail adder,' conducted a hearing on whether the Commission should adopt the terms of the Proposed Settlement. The parties

who joined the Proposed Settlement are Staff, the Division of the Public Advocate ('DPA'), DP&L, Conectiv Energy Supply, Inc. ('CESI'), and Delaware Energy Users' Group ('DEUG ') (collectively, 'Settling Parties'.

9. On August 1, 2004, I conducted the public comment portion of the hearing, as noticed by newspaper publication, press release, and direct contact with Delmarva's Project Concern participants. [11] Leslie Lee, who administers the low-income home energy assistance program for the Division of State Service Centers of the Department of Health and Social Services, was the only non-party to appear. She asked several procedural questions but offered no public comment.

10. On August 4, 2005, after postponing the evidentiary portion of the hearing in order to allow the parties more time to negotiate changes to the Proposed Settlement in an effort to secure full consensus among the parties, I conducted the remainder of the hearing. At the hearing, the Settling Parties each appeared in support of the Proposed Settlement while Retail Energy Marketers' Association ('RESA'), Select Energy, Inc. ('Select'), Strategic Energy, LLC ('Strategic'), and Premcor Refining Group ('Premcor') opposed the Proposed Settlement. [12] The record, as developed at the hearing, consists of a 680-page verbatim transcript and ten exhibits.

11. On August 16, 2005, in accordance with the approved post-hearing schedule, certain parties filed post-hearing briefs. Staff, DPA, Delmarva, and CESI each filed briefs supporting the Proposed Settlement. Three of the retail marketers that participated in this proceeding, RESA, Select, and Strategic (collectively 'Retail Marketers') jointly filed one brief opposing the Proposed Settlement. [13] I have considered all of the record evidence as well as the post-hearing briefs and, based thereon, I submit for the Commission's consideration this Report of the Hearing Examiner.

III. THE PROPOSED SETTLEMENT

12. A summary of the terms of the Proposed Settlement (Ex. 2), taken largely from Staff's in its brief, is as follows.

13. The Proposed Settlement provides that Delmarva will provide SOS to all customer classes, with no specified termination date. There will be two categories of SOS: (1) a fixed price service ('FPS') available to all but the largest customers (*i.e.*, the eleven GS-T customers, who all take at a transmission level voltage); and (2) an hourly priced service ('HPS') that is mandatory for GS-T customers and will be offered as an option for GS-P customers (generally, the large commercial customers). In order to take HPS, a GS-P customer must make an affirmative election prior to the Request for Proposal ('RFP') process for selecting wholesale SOS providers, and must have an interval meter or be willing to pay for installation of such a meter prior to beginning HPS. GS-P customers will have the opportunity to elect HPS or FPS every year. [14] All other SOS customers must take the FPS.

14. Under the Proposed Settlement, a competitive RFP process will be used to procure the full requirements of customers eligible for a fixed price SOS. Bidders will be asked to bid seasonally, but the retail rates will be developed using the bids and converting them into the existing rate design structures. In consultation with the other parties in this docket, Delmarva is in the process of developing a Full Requirements Service Agreement ('FSA') and an RFP (collectively, a 'Bid Plan'). The proposed settlement calls for a consultant selected by the Commission to monitor and participate in the bidding process. The Company will pay for the consultant, with the expenses being recovered in charges that are part of the fixed price SOS. That consultant, as well as the DPA and its consultant, will be permitted unfettered access to the bid process, subject to confidentiality concerns.

15. To provide rate stability for residential and small commercial customers, Delmarva will initially procure 1/3 of the load with a three-year contract (which will actually be 37 months for the first three-year contract), 1/3 with a two-year contract (which will actually be 25 months for the first two-year contract), and 1/3 with a one-year contract (which will actually be 13 months for the first one-year contract). [15] By the end of the second year, there will be a portfolio of three-year contracts to serve this load, and each

year thereafter, a new three-year contract for 1/3 of that load will be entered into to replace the expiring one. One-year contracts will be used for all other customer classes eligible for the fixed price SOS.

16. Under the Proposed Settlement, there are two major components of the SOS retail supply rates. First is the Full Requirements Costs ('FRC'), which, with the exception of the Volumetric Risk Mechanism ('VRM'),[16] is comprised of the costs that Delmarva pays to the winning bidders. Absent a Commission finding of exceptional circumstances, the FRC component will be reset and fixed for 12 months. The FRC will be trued up annually, and this will result in the retail rate for SOS being reset on an annual basis.

17. Under the Proposed Settlement, the 'reasonable allowance for retail margin' ('RARM') mandated by the Restructuring Act is comprised of the following components:

***8** (1) Incremental expenses incurred:

(a) to provide fixed price SOS and HPS;

(b) to administer the VRM applicable with respect to fixed price SOS customer load; and

(c) carrying costs on Cash Working Capital for fixed price SOS and HPS;

(2) $2.75 million per 12-month period, which for the Year 1 and Year 2 rates, is deemed to include any carrying costs on incremental capitalized costs associated with providing fixed price SOS and the VRM, but does not include the separately-calculated carrying costs for capitalized billing system software costs needed to bill and track HPS costs and revenues and also does not include any return on investment that is removed from distribution rates as supply-related; and

(3) For GS-T customers and those in the GS-P class that have elected HPS, the allocable share of the above categories plus an amortized amount, including carrying costs on the unamortized balance of the capitalized billing system software costs and interface costs needed to bill and track HPS costs and expenses.

18. In the event that investment is removed from distribution rates in a future distribution base rate proceeding as supply-related, the RARM shall include a fourth component comprised of the rate necessary to recover the same revenue requirement components as would have been applied if such investment were to have remained in distribution rates (*e.g.*, depreciation expense and return on investment grossed-up for taxes). Such an adjustment to the RARM shall be made without regard to any other cost component.

19. Delmarva will establish the incremental costs of providing SOS by conducting a lead-lag study to determine its cash working capital requirements. The calculation of these requirements will use Delmarva's total weighted cost of capital grossed up for income taxes. Delmarva will apply its grossed-up cost of capital to the results of the lead-lag study to determine its cash working capital requirements in mills per kWh for each customer class. It will estimate its other incremental capital costs and expenses and provide the Staff and DPA with the supporting workpapers, documents, cost centers and internal work order numbers that Delmarva uses to collect and track costs. These estimates will be reconciled in a proceeding that will be held after actual cost data are known. After this one-time reconciliation, the RARM will remain fixed unless changed by the Commission.

20. The Proposed Settlement also permits Delmarva to implement a pass-through mechanism pursuant to which its retail transmission rates will be developed and billed on the same basis that PJM and FERC use to develop rates and bill Delmarva for transmission. Currently, Delmarva's Delaware transmission rates are designed so that in the aggregate, they collect what PJM charges Delmarva. PJM, however, uses peak load capacity as a billing

determinant while Delmarva uses monthly demand for larger retail customers and kWh usage for residential and smaller commercial and industrial customers. The settlement proposal reduces the potential for mismatches between FERC costs and retail rate recovery and provides an incentive for customers to participate in demand response programs.

21. As of May 1, 2006, all residential customers and all commercial, industrial, governmental and other customers other than GS-T customers and electing GS-P customers will be eligible for fixed price SOS.[17] SOS rates will vary by customer type because the prices will be based on the winning bids received from wholesale suppliers under an RFP bidding process. The supply requirements for residential and the smallest non-residential customers will be bid out as one group. MGS-S customers will form another group, and their load will be bid separately. LGS-S customers will form a third group, and non-electing GS-P customers will comprise the fourth group. (Exs. 2, 3.)

IV. SUMMARY OF EVIDENCE

22. Testimony in support of the Proposed Settlement (Ex. 2) was pre-filed (and adopted as sworn testimony) by DP&L witness Schaub (Ex. 3), DEUG witness Alan Rosenberg (Ex. 4), CESI witness Champe Fisher (Ex. 5), DPA witness Andrea C. Crane (Ex. 6), Staff witness Janis L. Dillard (Ex. 8), and Premcor witness Jay Fuess (Ex. 9). The following is a summary this pre-filed testimony as well as the live testimony from the hearing (as provided, in large part, by Delmarva in its brief).

23. Mr. Schaub summarized the Proposed Settlement and concluded that adoption thereof would be in the public interest. (Ex. 3 at 2, 6-9; Tr. 393-96.) He identified several specific elements of the Proposed Settlement that were beneficial to customers, including that:

*9 a) Delmarva will provide SOS under PSC regulation;

b) Wholesale procurement of SOS is a proven method to obtain fair market prices;

c) The structure of the procurement is modeled after successful programs in other states, and a similar process has received affirmation from FERC;

d) Customers may shop at any time if that is to their advantage and can therefore have the benefits of retail choice;

e) Customers most inclined to shop will have SOS prices reset annually to reflect market conditions thereby allowing more contemporary pricing offers from third party suppliers;

f) The largest customers may take advantage of volatile hourly pricing if they are able to manage the volatility to their benefit;

g) Residential and small commercial customers are provided less volatile pricing through longer term procurement because price stability is most important to them;

h) Delmarva's experience with performing similar procurements means low incremental expenses associated with procurement and related functions; and

i) The wholesale market has proven quite competitive when similar procurements have been conducted.

(Ex. 3 at 2-3.)

24. Mr. Schaub further identified elements of the Proposed Settlement that were beneficial to wholesale suppliers of power, retail marketers, and DP&L. (Ex. 3 at 3-4.) He noted that the Proposed Settlement reflected compromise by each of the Settling Parties and asserted that the Settling Parties aggressively represented customer interests. (Ex. 3 at 5.)

25. In oral surrebuttal, Mr. Schaub responded to comments filed by Premcor regarding whether Premcor should have to pay for services that it does not intend to use. Mr. Schaub explained that Delmarva was legally obligated to provide SOS to Premcor. (Tr. 398.) Because there are fixed costs that are incurred to stand ready to serve hourly priced service (HPS) customers, Mr. Schaub concluded that Premcor should pay a share of those fixed costs irrespective of whether or not Premcor availed itself of that service. (Tr. 398-99.)

26. Mr. Schaub also responded to Select's alternative proposal for how the SOS procurement process should be implemented and rates set and identified several reasons for rejecting that proposal. He noted that Select's proposal was unacceptable to the Company because it would cause existing rate classes to be split into different groups based on size, causing additional administrative expenses for the Company. (Tr. 400.) Additional administrative burdens were proposed in the form of quarterly procurement cycles, which Mr. Schaub opposed because there 'doesn't seem to be any benefit accruing to customers that justifies that incremental cost.' (Tr. 401.) Mr. Schaub also opposed Select's proposal to deny fixed price SOS to larger customers in the GS-P and LGS-S classes, noting that 'we're certainly not hearing any interest in that from the representatives of those customers.' (Tr. 400-01.) He also testified that for residential and small non-residential customers, the use of rolling three-year contracts as set forth in the Proposed Settlement rather than the one-year contracts proposed by Select, 'satisfies the needs of those customers for some rate stability over time while still providing a market base[d] price.'' (Tr. 401-02.)

27. DEUG witness Rosenberg testified that DEUG was comprised of industrial customers taking service primarily under the GS-T and GS-P service classifications and that the Proposed Settlement met the objectives of the DEUG members to establish an appropriately priced hourly priced service for the customers who were sophisticated enough to want such a service while not mandating such a service for the GS-P customers; many of whom may be less sophisticated. (Ex. 4 at 3.) Dr. Rosenberg noted the benefits to industrial customers from having no minimum stay or other requirements limited customers' ability to move between a Delmarva provided supply service and a supply service from a competitive retail marketer. (*Id.* at 4.) He testified that the provisions that change the way transmission and ancillary rates are charged for retail purposes to use the same billing mechanisms that PJM uses to charge Delmarva will promote demand side management. (*Id.* at 5-7.) He supported the pricing mechanisms established for the HPS, including how the HPS billing system costs would be recovered from HPS customers. (*Id.* at 9-12.) He concluded that the Proposed Settlement was in the public interest and should be approved. (*Id.* at 14.)

28. CESI witness Fisher testified that the sections of the Proposed Settlement that deal with the way in which Delmarva will acquire the supply required to meet its SOS supply obligations are in the public interest. (Ex. 5 at 3.) In particular, Mr. Fisher supported the RFP process set forth in the Proposed Settlement and the use of a Volumetric Risk Mitigation ('VRM') mechanism that should operate to encourage active participation in the RFP process by wholesale sellers of electricity. (Ex. 5 at 3-5.) On the stand, Mr. Fisher testified that a wholesale bid from CESI would be higher to a retailer under an agreement that did not contain a VRM than it would be to a retailer under an agreement with a VRM. (Tr. 480-81.) He also noted that standard contract provisions between CESI and retailers contain alternative mechanisms for limiting CESI's risk. (Tr. 484-85.)

29. DPA witness Crane testified that the Proposed Settlement was in the public interest and should be approved. (Ex. 6 at 5.) She further testified that:

*10 On balance, I believe that the Settlement provides a fair and reasonable resolution of the issues in this case. The Settlement provides a competitive process for procuring electric generation supply. Moreover, it allows Delmarva to recover its actual procurement costs as well as the incremental administrative costs of providing SOS. In this regard,

the Settlement is consistent with the statute, since it ensures that the SOS price will be 'representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin ....'

The Settlement also provides some rate stability to customers, particularly residential and small commercial customers who will receive SOS procured through three-year contracts. Additional stability will be provided after Year 2, when the RARM is reset, since the settlement does not provide for annual changes to the RARM after the Year 1 true-up. The Settlement also avoids the 'residual charge' proposed as part of Delmarva's Administrative Charge, which in my opinion would have inflated SOS rate without providing any attendant benefit to customers. Finally, the Settlement will avoid the need for protracted and expensive litigation. Avoiding such litigation is especially important given the fact that the SOS process must be in place by May 1, 2006.

(*Id.* at 12.)

30. Ms. Crane, in oral surrebuttal, testified against Select's recommendations. In particular, she opposed Select's proposal to 'restrict choice by requiring an hourly price service for all customers over six hundred kW by year two.' (Tr. 490.) She also noted that Select's proposal would increase costs by requiring four rounds of bids each year and by splitting rate classes by size. (Tr. 490-91.) She noted that while some costs involved in the RFP process may be one-time set up costs, other costs, such as the $75,000 in estimated costs for an outside consultant reporting to the Commission to oversee the RFP process, would be incurred multiple times per year under the Select proposal. (Tr. 514-16.) She also testified against a so-called 'retail adder" that was included in the Company's originally filed proposal and in Select's proposal, but is not incorporated in the Proposed Settlement. (Tr. 491.)

31. Staff witness Dillard testified that the Proposed Settlement was in the public interest and should be approved by the Commission. (Ex. 8 at 3.) Ms. Dillard identified in her pre-filed testimony and on the stand several specific aspects of the Proposed Settlement that benefited customers, wholesale marketers, and retail marketers. She noted that the RFP process in the Proposed Settlement was a 'fairly low-cost way for a small state like Delaware to conduct the procurement process' and that a lot of time was spent 'dealing with cost recovery because we wanted to make sure the company was able to recover all of its real costs of providing the SOS service, but wasn't going to be able to double recover any cost.' (Tr. 521-22.) Ms. Dillard pointed out several specific provisions that benefited retail marketers including that there would be no minimum stay requirements that would restrict customers moving back-and-forth between shopping competitively and returning to SOS; that making hourly priced service mandatory for GS-T customers and optional for GS-P customers provides an opportunity for retail marketers to offer a fixed price alternative; that by ensuring that all incremental costs are going to be in the shopping credit, retail suppliers will have some 'head room to compete;' and that the power procured for the SOS provided to medium-sized non-residential customers would be done under one-year, rather than two-year, contracts. (Tr. 522-23.)

32. On the stand, Ms. Dillard explained at some length the process by which the Proposed Settlement was reached. She described the workshop process and Staff's efforts to develop a comprehensive settlement package, which would address the concerns raised by all parties, including the retail marketers. (Tr. 525.) She explained the efforts that Staff made to identify areas of common interest that could form the basis of a settlement and how those discussions started with DPA, then expanded to include the Company and then DEUG. (Tr. 523-24.) After noting various instances where she had had discussions with retail marketers, she concluded that retailers had a fair opportunity to participate in the process, testifying that:

*11 [W]e talked to them through the workshops. We talked to them on May 31st. I talked to them in June. We had a lot of discussions in the week after the settlement was filed. So, I think they had an adequate opportunity to air their views. I think it was more just a disagreement on policy, the way that we thought Delaware should go on these issues.

(Tr. 531.)

33. Premcor submitted a letter (Ex. 9), adopted on the stand by witness Jay Fuess, in opposition to the Proposed Settlement. The letter stated that while Premcor participated in the workshop process, nothing discussed therein appeared to affect Premcor and that Premcor was surprised by the draft of a settlement sent to it on July 7, 2005, which had the result of assigning a sizable portion of the costs of Delmarva's hourly billing system costs to Premcor. In Premcor's view, this was inappropriate because Premcor does not take its supply service from Delmarva and would never benefit from the use of the hourly billing system. (Ex. 9 at 2.) On the stand, Mr. Fuess also made an assertion that he thought that Premcor's bills were so complex that he thought it likely that even if Premcor were to take service from Delmarva, the bills would need to be done manually, and not through the hourly billing software. (Tr. 559.) Premcor also raised concerns regarding the process by which the July 7, 2005 draft settlement was developed, without input from Premcor. (Ex. 9 at 1-2.)

34. Select presented two witnesses as a panel, Messrs. Marc Hanks and Leonard Navitsky, who testified in opposition to the Proposed Settlement. Their pre-filed testimony stated that Select had not been consulted with during the settlement process, which they characterized as 'private negotiations,' and that 'Select first became aware of the 'Proposed Settlement' when we were provided a copy on July 7 and were given a mere two days to provide comments.' (Ex. 10 at 4.) Select's witnesses testified that the Proposed Settlement will hamper the development of a competitive market because it continues 'to mask the true cost of electricity from consumers.' (*Id.* at 5.) Select's witnesses then presented an alternative proposal. The alternative proposal would increase the number of customers for whom only the HPS form of SOS would be available, ultimately resulting in all customers with peak loads in excess of 600 kW being eligible for only the HPS form of SOS. (Ex. 10 at 6-7 and 9.)

35. Select also proposed that Delmarva procure power every quarter through an RFP process to serve customers with peak loads above 100 kW and that annual RFP's be used with contracts not to exceed a term of one year for residential and smaller non-residential customers. (*Id.* at 8.) In the third year of the program, Select would require a new proceeding be initiated to propose changes for implementation in the fourth year. (*Id.* at 9.) Select also proposed that the retail prices charged by Delmarva to its SOS customers include additional retail margins. (*Id.* at 10-12.) The bases for this proposal were that there are retail adders on some or all customer classes in surrounding states and that Delmarva's initial pre-filed testimony in this proceeding (*i.e.*, prior to the Proposed Settlement agreement was reached) proposed retail margins. (*Id.*)

36. On cross-examination, Mr. Navitsky agreed that Select did not review the underlying Delmarva records or documents that formed the basis for the pre-filed testimony, that the panel was unaware of the risks identified in that testimony with respect to the operations of Delmarva's New Jersey utility affiliate, and that they had not independently verified the data presented. (Tr. 610-11.)

V. DISCUSSION

37. In Stage 1 of this docket, the Commission selected Delmarva as the SOS provider for its service territory and decided that Delmarva would provide SOS service under the 'wholesale' model. (Order No. 6598 (Mar. 22, 2005).) In this stage, the Commission will develop a procedure under which Delmarva will procure, provide, and price the SOS supply. In Stage 3, the Commission will select the wholesale providers and determine the post-May 2006 SOS prices, in accordance with the procedures and pricing mechanisms developed in this stage.

38. After numerous workshops, written and oral comments, off-line discussions, and protracted negotiations, Staff, DPA, DP&L, CESI, and DEUG reached an agreement as to all Stage 2 issues, as outlined above. RESA, Select, and Strategic (collectively 'Retail Marketers') and Premcor oppose the Proposed Settlement, despite Staff's attempts, both before and after the hearing, at reaching a full consensus. As outlined below, however, I recommend that the Commission approve the Proposed Settlement in this case because it complies with the Restructuring Act and its adoption would be in the public interest.

39. The Restructuring Act provides that the Commission shall determine who will provide SOS and that the Commission is permitted, but not required, to designate Delmarva as the SOS provider.[18] As noted above, the Commission has already selected Delmarva to continue as the SOS provider for its service territory. (Order No. 6598.) The Restructuring Act further provides[19] that:

*12 If DP&L is a standard offer service supplier, the standard offer service price shall be revised by DP&L from time to time for each customer rate class to be representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin to be determined by the Commission for providing such electric supply service. The standard offer service price may be reviewed from time to time by the Commission to determine whether it represents the regional wholesale electric market price, plus a reasonable allowance for retail margin.

The Restructuring Act, therefore, directs the Commission to determine an SOS price that is 'representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin.'

40. The Proposed Settlement meets each of these requirements. The power for SOS will be acquired at a price 'representative of the regional wholesale electric market price' because Delmarva will obtain the power either through PJM's competitive markets (in the case of the HPS SOS) or through a process where wholesale bidders, acting in their own self interest, will bid competitively. Furthermore, the integrity of the procurement process is assured by the oversight of an outside consultant who will monitor the process and report to the Commission. (Delmarva Br. at 20-22.)

41. The Proposed Settlement also explicitly contains a 'reasonable allowance for retail margin' ('RARM'), which includes Delmarva's incremental cost of providing SOS (to be determined in Delmarva's upcoming distribution rate case), plus a component for return, or profit. The RARM also contains a true-up provision to capture costs to the extent not identified or recovered in the first year's rates and further contains a 'catch-all' provision to capture any category of cost that may have been overlooked.

42. In addition, the record amply supports a finding that adoption of the Proposed Settlement would be in the public interest. Pursuant to Section 512 of the Public Utilities Act, the Commission may approve a settlement where the Commission finds the settlement to be in the public interest, whether or not all parties have joined the settlement. More specifically:

Insofar as practicable, the Commission shall encourage the resolution of matters brought before it through the use of stipulations and settlements.

The Commission's staff may be an active participant in the resolution of such matters.

The Commission may upon hearing approve the resolution of matters brought before it by stipulations or settlements whether or not such stipulations or settlements are agreed to or approved by all parties where the Commission finds such resolution to be in the public interest.

26 Del. C. §512 (a)-(c).

43. First, it is significant that the Settling Parties, all of whom maintain that the Proposed Settlement is in the public interest, represent a wide variety of interests. Staff represents the interests of ratepayers and regulated utilities. DPA represents all ratepayers, but focuses primarily on residential and small commercial customers. DEUG represents certain large industrial customers (including members of the GS-T class, which is the only class subject to the mandatory HPS form of SOS). CESI's interest in this proceeding is as a potential

wholesale provider of service, *i.e.*, a prospective bidder in the RFP process to supply Delmarva with power for the SOS. And, of course, Delmarva is the SOS provider and local distribution company for its territory.

44. The public interest argument in support of the Proposed Settlement would, of course, be stronger if the Retail Marketers joined the agreement. After all, one goal of the Restructuring Act is to encourage retail competition, and whether retail competition takes hold in Delaware will depend on the business decisions and future success of retail marketers in Delaware. On the other hand, the Commission should also consider that retail marketers will be competing directly with the SOS provider and, therefore, have a direct interest in making the SOS service as unattractive as possible in order to increase their chances of gaining market share. Not surprisingly, their positions in this case, as discussed below, support changes to the Proposed Settlement that would raise the price of SOS and limit the options available to SOS customers.

45. In addition, the Retail Marketers' opposition to the Proposed Settlement should not be interpreted to mean that their interests were not considered. In fact, the Settling Parties included in the Proposed Settlement several terms that benefit retail marketers. (Ex. 8 (Dillard) at 14-15; Ex. 3 (Schaub) at 4, Tr. 522-23 (Dillard.)) Such terms include the annual resetting of rates (to better reflect current market prices), the elimination of returning customer rules (so that customers may leave SOS without fear of not being able to return to SOS), the addition of the RARM, which includes a profit margin, on top of wholesale prices (to provide 'headroom' under which competitors can price their services), and restructuring how Delmarva charges for transmission and ancillary rates to correspond more closely with how PJM charges retail marketers for such services (to enhance a marketer's ability to match its price components with the SOS pricing).

46. The Retail Marketers argue, however, that the Proposed Settlement should not be adopted unless modified (1) to require HPS for all large commercial and industrial customers (rather than just the eleven GS-T customers) and (2) to increase the RARM to be more reflective of 'actual' cost, which, according to the Retail Marketers, is better reflected by Delmarva's initial, pre-settlement position.[20] (RM Br. at 6-20.) According to the Retail Marketers, adoption of the Proposed Settlement without these modifications would run contrary to the public interest and to the Restructuring Act because the resulting SOS product and pricing would discourage shopping and would, therefore, prevent the development of retail competition in Delaware.[21]

47. Regarding the Retail Marketers' first point, the Proposed Settlement requires the eleven GS-T (transmission-level) industrial customers to take HPS, allows the larger GS-P customers (with interval meters) to choose HPS (or default to FPS), and requires all other SOS customers to take FPS. The Retail Marketers argue that more customers should be restricted to HPS because HPS is more responsive to market conditions than FPS and because such a restriction would benefit competition by forcing those customers who wanted a fixed price service to switch to a competitive supplier. (RM Br. at 7-8.) In response, the DPA makes the following pertinent observation:

***13** Although Select argues that HPS provides better price signals to customers, Select admitted that it has no Delaware customers taking HPS. It is ironic that Select is promoting implementing HPS in Delaware, even though none of its customers in Delaware take HPS. (Tr. 592.) Clearly, Select does not need DP&L to offer an HPS so that it can be put on a level playing field with DP&L because Select itself has no customers on HPS. Select's proposal to increase mandatory HPS appears to be simply a ploy to drive customers away from SOS. DPA witness Crane explained in her testimony that it would be Select, and not Delaware ratepayers, who would benefit under Select's proposal.

In addition, even if further restricting SOS FPS somehow benefited competition, any such benefit is outweighed by the interests of the affected customers who wish to remain on SOS but who seek the price stability of a fixed price service. After all, even the DEUG witness, who supports HPS for large sophisticated customers, noted that some large customers may not find HPS attractive 'because of its volatility, which can create budgeting chaos and uncertainty ....' (Ex. 4 (Rosenberg) at 14; Delmarva Br. at 26.)

48. Regarding the Retail Marketers' second point, the RARM consists of Delmarva's incremental cost of providing SOS, which will be determined in Delmarva's upcoming distribution rate case (and which will be subject to a true-up), plus a $2.75 million return component. The Retail Marketers argue that without placing a number figure on the incremental costs in this proceeding, and without evidence to show that the $2.75 million actually covers Delmarva's cost of capital associated with incremental SOS investment, adoption of these terms would not be legally sustainable, because they are not based on substantial evidence. (Retail Marketers Br. at 13-20.)

49. First, the Settling Parties' witnesses testified that the proposed RARM cost components will cover Delmarva's incremental costs and that the proposed return will satisfy the statutory requirement for a 'reasonable' retail margin. (Ex. 3 (Schaub) at 4; Ex. 8 (Dillard) at 9; Ex. 6 (Crane) at 12; Tr. at 489 (Crane); Ex. 4 (Rosenberg) at 2-3.) This expert testimony certainly constitutes record evidence in support of these terms. Second, while it can shown that Delmarva's litigation position (now espoused by the Retail Marketers) included somewhat larger profit margins, that is not the same as establishing that the profit margins reflected in the Proposed Settlement are not adequate or somehow fail a statutory requirement by not encouraging competition. Moreover, as argued by Delmarva, the parties contesting a settlement in Delaware do not have the right to a full trial on their issues. [22] Instead, the adjudicator of a contested settlement need only know enough about the merits of the settled issues and the identity of the parties to the settlement to be able to evaluate the settlement. [23] (Delmarva Br. at 29-30.)

50. Furthermore, even if the Commission fully litigated Delmarva's incremental cost of providing SOS and its associated cost of capital, complete with cost studies and cost of capital expert testimony, the parties' positions would still diverge substantially (consistent with their self-interests) and determination of the 'correct' numbers would remain elusive. After all, the parties' litigated positions would depend largely on their views of cost allocation and risk valuation, over which experts often (and inevitably) disagree. As such, avoiding the considerable cost of a fully litigated proceeding, which would carry uncertain benefit, further supports a conclusion that adoption of the Proposed Settlement is in the public interest.

51. Premcor's objection is based primarily on the fact that it believes that Premcor should not pay for the cost of a system that it is not currently using. (Staff Br. at 23-24.) But as Mr. Fuess conceded at the evidentiary hearing, if in the future Premcor's load serving entity ('LSE') was no longer qualified as an LSE by PJM, it 'would probably have to fall back to Delmarva.' (Tr. at 567.) As explained by Delmarva witness Schaub, Delmarva is obligated to provide supply to Premcor under HPS at any time should Premcor request Delmarva to do so. (Tr. at 399.) The costs that Premcor will be responsible for are the costs of setting up the hourly billing system, which will exist whether or not Premcor takes the service initially or not. (Tr. at 399-400.) For these reasons, Premcor is responsible for such costs and the Commission should not reject the Proposed Settlement on the basis of Premcor's objection.

VI. RECOMMENDATIONS

52. In summary, and for the reasons discussed above, I propose and recommend to the Commission the following:

***14** A. That the Commission find the attached Proposed Settlement ('Attachment A ') to be in the public interest and in compliance with state law and, therefore, adopt it as a resolution of the Stage 2 issues in this docket; and

B. That the Commission initiate Stage 3 of this docket for the purpose of selecting the wholesale providers for SOS and determining the post-May 2006 SOS prices, in accordance with the procedures and pricing mechanisms set forth in the Proposed Settlement.

Respectfully submitted,

William F. O'Brien William F. O'Brien Hearing Examiner

Dated: September 1, 2005

ATTACHMENT 'A'

PROPOSED SETTLEMENT

On this day, July 14, 2005, the undersigned, all of whom together are the 'Parties' or 'Settling Parties,' hereby propose a complete settlement of all issues that were raised in this proceeding, except as specifically reserved for a subsequent proceeding or phase of this proceeding.

I. INTRODUCTION AND PROCEDURAL BACKGROUND

On October 19, 2004, this proceeding was initiated by Delaware Public Service Commission ('DPSC' or the 'Commission') Order No. 6490. The Order discusses certain statutory requirements and prior cases involving the provision of standard offer service to customers of Delmarva Power & Light Company ('Delmarva'). The Order also established a process under which various major policy issues would be resolved in an initial phase of the proceeding, while other policy and technical issues would be resolved in one or more subsequent phases of the proceeding. On March 22, 2005, in Order No. 6598, the Commission reviewed a report and recommendation presented by the Staff of the Commission ('Staff'), which report and recommendation was the subject of written comments and oral argument presented by interested parties to the proceeding. As described more thoroughly therein, Order No. 6598 resolved certain major policy issues. Order No. 6598 also outlines the history of this proceeding through March 22, 2005.

Subsequent to March 22, 2005, the parties to the proceeding have met on several occasions in informal workshops, open to the public, to discuss remaining issues in the proceeding. Various parties have also met privately to attempt to reach a settlement of some or all of those remaining issues.

A procedural schedule was approved by the Hearing Examiner, modified to provide more time for settlement discussions.

The Division of the Public Advocate ('DPA') made a timely notice to participate in the proceeding. In addition to the Company, Staff, and DPA, other parties to the proceeding as of July 7, 2005 are: the Delaware Energy Users Group ('DEUG'), PROPOSED SETTLEMENT Energy Resources & Trade LLC, Select Energy, Inc., Strategic Energy, LLC, Constellation Energy Commodity Group, Inc. and Constellation New Energy, Inc., Washington Gas Energy Services, Inc., PEPCO Energy Services, Inc., Conectiv Energy Supply, Inc., the Delaware Electric Cooperative, and PJM Interconnection, LLC.

II. SETTLEMENT PROVISIONS

A. Definitions.

***15** 'Actual incremental costs' are defined as additional costs incurred by Delmarva for reasons other than waste, bad faith, or an abuse of discretion, as a result of providing FP-SOS and HPS (including any 'Inc' amounts) that are not included in distribution rates. For example, such actual incremental costs include: uncollectibles that are not being recovered in Delmarva's distribution rates; consultants; procurement processes; incremental system costs; bill inserts for education; and transactions costs; and the cash working capital revenue requirement.

'Customer' shall have the same meaning as in the Delmarva Delaware retail tariff.

'Customer group' or 'customer grouping' is used herein to identify and group customer classes that will be treated similarly. For purposes of this settlement, customers within the R, R-TOU, R-TOU-SOP, SGS-ND, OL, ORL, X classes

and that portion of the load of customers with separately metered space heating and separately metered water heating comprise one customer group. Customers within the MGS-S class are a separate customer group. Customers within the LGS-S class are a separate customer group. Customers within the GS-P class are a separate customer group. Customers within the GS-T class are a separate customer group.

FP-SOS means fixed price standard offer service.

Full Requirements and Full Requirements Service shall have the meanings set forth in the form of Full-Requirements Service Agreement ('FSA').

Full Requirements Costs shall mean the total of all amounts paid to the supplying counterparties of FSAs.

HPS means hourly priced service, a form of standard offer service.

Inc, Inc load, Inc service and similar terms refer to the incremental service and loads to be supplied by Delmarva pursuant to a volumetric risk mitigation mechanism that operates with respect to customers in the LGS-S and GS-P class when there has been a defined threshold increase in load associated with customers from these classes beyond the obligations assumed by counterparties to FSAs.

R & Small C&I FP-SOS means the fixed price SOS that is available to customers served under service classifications R, R-TOU, R-TOU-SOP, SGS-ND, OL, ORL, or X, and separately metered space heating or water heating load.

SOS or Standard Offer Service is as defined in 26 Delmarva. C. § 1001 (15).

Year 1 means the thirteen month period of May 1, 2006 — May 31, 2007.

Year 2 means June 1, 2007 — May 31, 2008; subsequent Years are measured from June 1 of a given year through May 31 of the following year.

B. Standard Offer Service Availability.

1. Delmarva shall provide SOS to all classes of retail customers. As of May 1, 2006, an FP-SOS offering will be available for all customers other than customers served under the GS-T class. As of May 1, 2006, the form of SOS available to GS-T customers will be HPS.

2. In addition, GS-P customers will be eligible for HPS if: i) the GS-P customer makes an affirmative election to take HPS rather than FP-SOS; ii) such election is made by the GS-P customer no later than 45 calendar days prior to the date on which the first bid round occurs to provide Delmarva with supply for its GS-P customers taking FP-SOS; iii) the GS-P customer has an interval meter or will pay to have such a meter installed prior to the beginning of its HPS. No later than 30 calendar days prior to the deadline for making such an election, Delmarva shall send a letter to each GS-P customer informing such customers of the option to elect HPS and instructions as to how to make such an election. Such election shall be made annually and shall be effective for the entire year when made. The election shall be operative during any part of a Year during which the GS-P customer is receiving SOS, including a GS-P customer returning to SOS after previously receiving a supply service from a competitive retail supplier. An election or failure to make an election shall not affect the right of a GS-P customer to obtain its supply service from a competitive retail supplier. The failure to make an election in any given year will mean that a GS-P customer currently opting for HPS will be deemed to have elected HPS for the coming year, and a GS-P customer currently opting for FP-SOS will be deemed to have elected FP-SOS for the coming year.

C. Obtaining SOS Supply at Wholesale.

1. Request For Proposals Process.

*16 Delmarva shall obtain the Full Requirements necessary to provide FP-SOS through a competitively bid, Request for Proposals ('RFP') process. The contemplated RFP process will be described more fully in a Bid Plan that will be developed by Delmarva and submitted separately for review by the parties to this proceeding and for Commission approval. The elements of the Bid Plan are described more fully in Appendix A, which is incorporated herein by reference and made a part of this Settlement. As set forth therein, the RFP process will include oversight by a consultant selected by the Commission and accountable to the Commission, but paid by the Company, who will be permitted physical access during all portions of the process including the days that bids are received and evaluated. The DPA and its consultant will also be permitted such access. The Staff and DPA consultants will be required to execute a confidentiality agreement that is substantially similar to the form set forth in Appendix B. Such confidentiality agreement will not bar the consultant(s) from providing a report on a confidential basis to the Commission regarding the RFP process and evaluation of bids that includes the consultant's conclusions or recommendations to the Commission ...The Settling Parties recognize that there may be minor modifications that occur with respect to dates or procedures described in Appendix A or the Bid Plan. The Company will inform the Staff and DPA consultants of such minor modifications prior to the date that the consultant(s) report(s) would be made to the Commission.

2. Length of Contracts.

In Year 1, contracts with wholesale suppliers to serve the R & Small C&I FP-SOS load shall be executed such that one-third (1/3) of the projected load for Year 1 will be served under a thirteen month contract, one-third of the projected load for Year 1 will be served under a twenty-five month contract, and one-third of the projected load for Year 1 will be served under a thirty-seven month contract. In Year 2, only three-year contracts will be bid to serve one-third of the projected Year 2 load. The other two-thirds of the Year 2 projected load (which includes 2/3rds of the load growth relative to Year 1), shall continue to be served pursuant to the second year of the Year 1 two-year contracts and the second year of the Year 1 three year contracts. In Year 3 and thereafter, only three-year contracts will be bid out.

In Year 1, thirteen-month contracts with wholesale suppliers to serve the FP-SOS load of customers within the MGS-S, LGS-S and GS-P classes shall be executed to serve 100% of the projected load for Year 1. In Year 2 and thereafter, one-year contracts shall be executed. Separate contracts shall apply with respect to each of the customer groups MGS-S, LGS-S and GS-P.

The supply for HPS and for the 'Inc' service described below shall be obtained by Delmarva through PJM with energy procured at the Delmarva zonal real-time LMP as determined by PJM, capacity obtained through PJM's short-term capacity markets, short-term bilateral contracts, or at the capacity deficiency rate, or through any substitute capacity construct implemented by PJM, and ancillary charges as billed by PJM. The foregoing recognizes a degree of discretion on the Company's part with respect to how capacity is procured and the Company will exercise that discretion reasonably in an attempt to keep capacity costs in line with PJM prices for capacity available at the time a decision to procure capacity is made. Appendix C contains additional provisions relating to the HPS.

3. Pricing of Supply Contracts.

*17 The Bid Plan shall include instruction that bidders are required to bid for FP-SOS with a flat per kwh bid, which may vary by season, but would not change over the length of the contract, including those contracts that are for terms greater than one year.

D. Computation of Retail Supply Rates Generally.

1. The rate components for retail supply rates shall be as follows: a) the Full Requirements Costs incurred pursuant to the Full Requirements contracts entered into to serve the FP-SOS load for the particular customer class or grouping or, alternatively, the costs of acquiring energy, capacity and ancillary services for those customers receiving HPS; and b) a reasonable allowance for retail margin ('RARM'). As detailed below, retail rates for customers receiving FP-SOS or HPS will also include retail charges designed to recover, on an aggregate basis, FERC-approved transmission and ancillary charges and any other PJM charges and costs incurred by Delmarva associated with the SOS obligation. In addition, retail rates for customers receiving FP-SOS or HPS will be charged applicable taxes and any other cost element directly related to either the FP-SOS or the HPS that may be identified in a subsequent proceeding and approved by the Commission for recovery.

2. The Full Requirements Costs component of the Retail Supply rates for each customer grouping receiving FP-SOS shall be established to recover fully, but not overcollect, the costs of the Full Requirements contracts entered into to serve the FP-SOS load for such customers. The Full Requirements Costs component of the Retail Supply rates for FP-SOS load shall remain fixed during each Year, absent a Commission order finding that exceptional circumstances exist to warrant a rate change during a particular Year. Retail Supply rates for GS-T customers and those GS-P customers that have elected HPS, shall be charged monthly based on the changes in costs incurred hour-by-hour to serve such customers. These monthly charges are to recover fully, but not overcollect, the costs incurred to obtain capacity, energy, and ancillary services for HPS customers.

3. Algorithms for each customer grouping shall be developed by Delmarva and will be made available to prospective bidders. These algorithms will show how a per kwh bid price for FP-SOS will be translated into retail rates for each customer class or type of customer. Staff, DPA and the Commission will have an opportunity to review and comment on the algorithms prior to their being finalized. This rate translation process shall be performed to retain to the maximum extent feasible the currently-authorized rate design differences applied to a particular customer class or type of customer to reflect seasonality, time-of-use, or demand/commodity components. Nothing herein precludes a Settling Party from proposing in some future proceeding rate design changes that would be implemented prospectively only. The Settling Parties agree, however, that even prospective rate design changes may need to be phased in so as not to significantly change the bases upon which a wholesale supplier may have bid for a three-year contract.

4. The RARM is comprised of the following components: a) incremental expenses incurred: i) to provide FP-SOS and HPS; ii) to administer the Volumetric Risk Mitigation (VRM) mechanism described below and applicable with respect to FP-SOS customer load; and iii) carrying costs on Cash Working Capital (CWC) for FP-SOS and HPS; b) $2.75 million per 12 month period, which, for the Year 1 and 2 rates, is deemed to include any carrying costs on incremental capitalized costs associated with providing FP-SOS and the VRM mechanism, but does not include the separately calculated carrying costs for capitalized billing system software costs needed to bill and track HPS costs and revenues and also does not include any return on investment that is removed from distribution rates as supply related; and c) for GS-T customers and those in the GS-P class that have made an election for HPS, the allocable share of the above categories plus an amortized amount, including carrying costs on the unamortized balance of the capitalized billing system software costs and interface systems needed to bill and track HPS costs and revenues. For illustrative purposes only, Appendix D shows how an illustrative amount of such costs would be recovered through amortization with carrying costs at an illustrative level.

5. In the event that investment is removed from distribution rates in a future distribution base rate proceeding as supply related, the RARM shall include a fourth component comprised of the rate necessary to recover the same revenue requirement components as would have been applied if such investment were to have remained in distribution rates (*e.g.*, depreciation expense, return on investment grossed-up for taxes, etc.) Such an RARM adjustment shall be made without regard to any other cost component and no Settling Party shall take a position that this fourth cost component should be reduced or offset in any way by the $2.75 million figure or some other RARM cost component. Nothing herein precludes

a Settling Party from asserting that the supply-related costs as removed from distribution rates should not be recoverable in the supply component of rates because such costs were incurred in violation of the statutory standard for recovery.

E. Setting Year 1 Retail Rates.

1. The incremental costs of providing SOS shall be initially established as follows.

*18 a) A lead lag study shall be performed by Delmarva and reviewed by the parties to determine the CWC requirements. The lead/lag study shall be performed in the following manner:

(1) Revenue lag will be calculated using the following components:

(i) mid-point of the service period to meter reading date;

(ii) meter-reading date to bill-rendered date; and

(iii) bill-rendered date to collection date.

(2) Lag in payment for electric supplier bills will be based upon the payment terms set forth in the FSA contained in the Bid Plan as approved by the Commission.

(3) Lag in payment of incremental costs will be determined separately for each category of cost.

(4) Lag in payment of all applicable taxes will be determined.

b) The calculation of cash working capital revenue requirement shall use the Delmarva's total weighted cost of capital grossed up for income taxes. The carrying costs on CWC shall be set to equal the overall rate of return that is established in Delmarva's upcoming distribution base rate case.

c) Delmarva will apply its grossed-up cost of capital to the results of its lead/lag study to determine cash working capital revenue requirements, in mills per kWh, for each customer group.

2. Delmarva shall estimate its other incremental capital costs and its other incremental expenses (including the reasonable costs incurred to administer the Volumetric Risk Mitigation (VRM) mechanism) and will provide to the Settling Parties the workpapers and other documentation underlying such estimates, including listing cost centers or Internal Order numbers that are or will be used to collect and track costs. Depreciation expense for the incremental capital costs will be based on a five year life unless a longer life is warranted for the particular type of equipment or asset involved. To the extent not deemed to be included pursuant to paragraph D.4 above, a return on incremental capital costs shall be set to equal the overall rate of return grossed up for income taxes that is established in Delmarva's upcoming distribution base rate case. Notwithstanding any other provision herein and irrespective of whether or not included in Delmarva's estimate of incremental capital costs or other incremental expenses, the incremental costs of providing SOS shall include any costs that are removed from Delmarva's distribution rates case in a Delmarva base rate proceeding if the basis for such removal is that such costs are supply-related.

3. Except with respect to GS-T customers and those GS-P customers who make a timely election for HPS, a 0.6 mill per kwh charge for each customer class or type of customer will be established initially to collect the net of the $2.75 million per 12 month period figure referenced in section D.4.b) minus the collections from GS-T customers and electing GS-P customers as set forth in the next sentence. GS-T customers will be charged instead a per-month charge of $400, which shall apply irrespective of whether the GS-T customer takes HPS or receives supply from a competitive retail

supplier. GS-P customers who make a timely election for HPS will be charged instead a per-month charge of $150, which shall apply irrespective of whether the electing GS-P takes HPS or receives supply from a competitive retail supplier.

4. A fixed annual amount of $175,000 shall be established as the costs referenced in section D.4.c). For GS-T customers and for GS-P customers who opt into HPS service prior to the beginning of Year 1, a fixed rate per month based on kW of PJM Peak Load Capacity will apply irrespective of whether or not the customer takes HPS.

*19 *F. Retail Rates for Transmission, Ancillary Services, HPS Capacity and HPS Energy.*

1. Effective June 1, 2006, and for each Year thereafter commencing on June 1, 2006, retail transmission rates shall be established such that, on an aggregated basis, such rates recover the same revenue as is charged by PJM to Delmarva for such transmission services. The Company shall endeavor to develop systems that will permit it to file and put into effect as early as June 1, 2006 and no later than June 1, 2007, retail transmission rates that are designed using the same formula rate structure, billing determinants, and other rate mechanisms as those reflected in the PJM transmission rates charged to Delmarva. The Parties recognize that a number of billing system and interface system modifications are already scheduled to accommodate regulatory requirements in other jurisdictions and to implement provisions in this Settlement. In the event that such system modifications are made, tested, and available for use prior to June 1, 2007, Delmarva shall notify the Commission and the Settling Parties and propose a prospective rate design change with an effective date prior to June 1, 2007.

2. Effective June 1, 2006, and for each Year thereafter commencing on June 1, 2006, retail ancillary rates shall be established such that, on an aggregated basis, such rates recover the difference, if any, between charges by PJM to Delmarva for ancillary services and the amounts paid by the wholesale suppliers on Delmarva's behalf or directly to PJM for ancillary services pursuant to the FSA.

3. Special Transition Rule for GS-T Customers. Effective June 1, 2006, GS-T transmission and ancillary service rates shall be redesigned as set forth above in sections F.1 and F.2. In the event that Delmarva has not at that time made the computerized system modifications necessary to implement such a rate design change, Delmarva shall implement procedures to bill GS-T customers manually.

4. To the extent not already recovered through PJM Network Integration Transmission Service charges and to the extent in effect when retail rates are reset pursuant to this Settlement, any existing PJM surcharges and any future surcharges assessed to network transmission customers for PJM-required transmission enhancements pursuant to the PJM Regional Transmission Expansion Plan, or for transition costs related to elimination of through-and-out transmission charges and other FERC-mandated changes in transmission rate design, will be included in the retail charges pursuant to this Settlement. Pursuant to the contemplated FSA, the wholesale suppliers shall bear the risk of any other changes in PJM products and pricing during the term of their FSAs, including changes in ancillary service charges or new ancillary service charges. In no event will Delmarva bear the risk of any changes in regulation or PJM rules related to such costs or charges.

5. In the event that there are any other new FERC-approved PJM transmission charges, or other new PJM charges and costs charged to network transmission customers, that Delmarva or any wholesale supplier believes should be recovered through retail rates because they are directly related to Delmarva's SOS obligations, then:

*20 a) Delmarva will file with the Commission, and provide notice to all Parties, a request for approval to recover such new charges through its retail rates. The wholesale supplier that brings the issue to Delmarva's attention will be required to intervene before the Commission. The Commission will resolve Delmarva's request on an expedited basis.

b) The wholesale supplier will bear the cost of all new PJM charges and costs that the Commission determines may not be recovered in rates by Delmarva. In no event will Delmarva bear the risk of any changes in regulation or PJM rules

related to such costs or charges. Also, in no event shall any PJM charges to other than network transmission customers be recovered through the Utility's retail transmission rates for service under the Settlement, except to the extent (if any) provided therein.

6. Retail charges for capacity for HPS customers shall be charged based on each customer's annual capacity obligation in accordance with (i) PJM's method of calculation, and (ii) PJM's monthly capacity auction closing prices for the applicable month, unless it is impracticable to obtain the full amount of capacity needed through the monthly capacity auction, in which case, the costs of obtaining capacity or capacity deficiency amounts would be reflected in the retail price. As an illustrative example, it is recognized that in the event of an unexpected competitive retail supplier default, a customer may be returned to Delmarva for HPS at a time when it would be too late to obtain capacity in the monthly capacity auction. Additionally, while the parties contemplate the use of the monthly capacity auction as the source of capacity for HPS customers, the parties recognize that if PJM eliminates the monthly capacity auction or significantly modifies the method by which capacity obligations are determined or met, this provision will be deemed to be modified as necessary to reflect those new PJM methods.

7. With the exception described in the next two sentences below, retail charges for energy for HPS customers and any 'Inc.' load shall be charged based on the PJM real time LMP for the Delmarva Zone. Customers taking HPS may elect, in accordance with PJM rules, to pay the nodal price for hourly energy; provided, however, that either PJM must charge Delmarva for such an electing customer's load at the nodal price for hour energy or that Delmarva will be permitted to recover any difference between the nodal price and the price charged to Delmarva via the annual true-up proceeding. The nodal price is determined by multiplying the customer's hourly load, adjusted for the applicable loss adjustment factor for the customer's service voltage level, with the hourly integrated LMP, or its successor, as determined and reported by PJM, at the specific bus or busses serving the customer's load.

G. Resetting of Retail Rates and True-Up Mechanisms For Year 2 and Thereafter.

1. As of the start of Year 2 and each Year thereafter, retail rates shall be reset to reflect:

***21** a) changes in projected Full Requirements Costs based on the Full Requirements Service Agreements that will be effective for such Year.

b) an adjustment to the Full Requirements Costs component to collect or return over the subsequent Year any differences between amounts billed to customers for FP-SOS and HPS (including any 'Inc.' amounts) and amounts paid to wholesale suppliers and PJM to provide the Full Requirements of FP-SOS and HPS (including any 'Inc.' supply) plus interest on the differences at a rate equal to the overall return established in Delmarva's next distribution rate case. Such differences shall be tracked on a monthly basis by customer grouping and would be subject to audit. The collection or return of differences plus interest shall be by customer grouping and thus, it is recognized that there may be circumstances in which one customer group is receiving a prospective downward adjustment while another group of customers is receiving a prospective upward adjustment. In each Year, the differences taken into account shall be based on the most recently available actual data. In the event that the estimated year-end balances become significant during a Year, Delmarva retains the right to request that the Commission approve an interim true-up to be effective prior to the end of the Year. It is the Settling Parties intent that HPS customers shall not be required to pay for costs that are related solely to the provision of FP-SOS.

c) Transmission and ancillary costs associated with providing SOS.

2. The Year 2 rates shall also include changes to the RARM amounts to remove non-recurring RARM costs reflected in the Year 1 rates, an annualized amount of RARM based on the then-known actual RARM costs incurred during Year 1, and known and measurable changes to RARM costs that will be incurred during Year 2.

3. Approximately four months after the start of Year 2, Delmarva shall submit documentation in this docket with copies to the Settling Parties, proposing revised rates to reflect a true-up of actual RARM costs incurred during the period between the start of this proceeding and the end of Year 1 and amounts billed to FP-SOS and HPS customers, *i.e.*, a true-up of costs and volumes. The differences plus interest (at a rate equal to the overall return established in Delmarva's next distribution base rate case), shall be collected from or returned to FP-SOS and HPS customers through a prospective rate adjustment over a time period to be established in that proceeding. Additionally, the millage rate charged to FP-SOS customers to collect the $2.75 million portion of the RARM, shall be reset in that proceeding based on actual annualized Year 1 (and known and measurable changes) of quantities of FP-SOS to be supplied annually. It is contemplated by the Settling Parties that the reset millage rate will be a single rate applied per kwh to all customers receiving FP-SOS in Year 2 and thereafter until changed. The fixed charge(s) for HPS customers designed to recover part of the $2.75 million portion of the RARM shall not be reset in that proceeding.

4. In the Year 2 proceeding described in section G.3., all Parties reserve the right to propose alternative methods for resetting rates if the procedures outlined in this subsection G would otherwise result in an extraordinary burden or unduly discriminatory result on customers. The following examples are intended to be illustrative but not exclusive examples of such events. For example, if rates would otherwise be reset such that virtually all the $2.75 million figure referenced above in section D. 4. b) were to be charged to residential customers because virtually all non-residential customers had chosen a competitive retail supplier in Year 1, parties could propose an alternative mechanism for Delmarva to recover the $2.75 million. As another example, if significant annual expenses were incurred associated with software licensing or administering the HPS, but only one or no customers were taking HPS, parties could propose an alternative mechanism for Delmarva to recover those expenses.

5. After the conclusion of the proceeding described above, there would be no additional changes to rates to reflect true-ups of RARM costs and FP-SOS and HPS volumes in any prior period, or to reset the millage rate to collect the $2.75 million portion of the RARM. Prospective changes in rates to reflect changes in RARM amounts and FP-SOS and HPS volumes, however, may be proposed at any time by any party. The proposed change in the RARM component of retail rates shall be considered by the Commission in a docketed proceeding that will be limited to a review of RARM components and collections of such components. The proposed charge shall go into effect within 60 days of filing or thereafter if a later date is proposed by the Company. Any change in such component of retail rates that goes into effect prior to a final order of the Commission shall be effective subject to refund including interest. In such a proceeding, no Settling Party will raise and all Settling Parties participating in the proceeding will not support any positions taken that such a rate change is inappropriate due to changes in non-RARM costs, revenues, or other factors (including cost of capital), or any costs or revenues associated with transmission, ancillary, or distribution services.

6. Notwithstanding anything that could be read to the contrary in sections G. 4 or 5 above, to the extent that the FP-SOS volume for the R & Small C&I customer group drops by more than 40% relative to the period June 1, 2006-May 31, 2007, any party may petition for prospective changes with respect to the recovery of a share from that group of the $2.75 million portion of the RARM. The form of such petition and the relief sought shall be in the discretion of the petitioning party and could, but is not required to, include proposals to reallocate to other customer groups the share of the $2.75 million charged to the R & Small C&I customer group, to modify how that share as allocated to the R & Small C&I customer group is recovered from that group, or to reduce the overall $2.75 million figure by some amount. Other parties may take any position with respect to such a petition in their sole discretion.

H. Volumetric Risk Mitigation Mechanism.

1. Subject to Delmarva's customer enrollment rules and tariffs and except as provided herein, effective May 1, 2006, there shall be no 'minimum stay' requirements for customers in any customer class that precludes a customer from obtaining service from a competitive retail supplier and returning to FP-SOS service and then subsequently obtaining service again from the same or another competitive retail supplier. If a GS-P customer elects to take HPS in a given Year and then takes service from a competitive retail supplier, any return to Delmarva's service shall be to the HPS during that Year. No volumetric risk mitigation mechanism is established herein with respect to customers other than those receiving FP-SOS that are within the MGS-S, LGS-S and GS-P customer classes.

***22** *2. Load Following Obligations and Exceptions.*

a) As will be more specifically set forth in a Full Requirements Service Agreement ('FSA') that is currently under development, each winning bidder ('Seller') will be required to execute the FSA (a 'Transaction') to supply FP-SOS and will be awarded a 'Bid Block' based on the Capacity Peak Load Contribution ('Capacity PLC'). Delmarva shall determine the Capacity PLC, stated in megawatts, associated with each Bid Block in each Transaction ('Base PLC Per Bid Block') as of the date of execution of each FSA. Subsequent to the determination of the Base PLC Per Bid Block, and on each Business Day (as defined in the FSA) thereafter, Delmarva shall determine the Capacity PLC, stated in megawatts, associated with each Bid Block in each Transaction ('PLC Per Bid Block'). The obligations of each Seller will include providing the Full Requirements of that Bid Block, including load following obligations, except as provided below and more specifically in the FSA.

b) Each Seller shall be obligated to provide full requirements service that follows load up to five (5) megawatts above the Base PLC Per Bid Block. If, on any day, the Capacity PLC of a Bid Block is greater than the Base PLC plus 5 MW an Inc Load of Capacity PLC less Base PLC Per Bid Block shall be triggered. When an Inc Load is triggered, the Seller will supply the full requirements service that follows load up to the Base PLC Per Bid Block plus 5 MW and Delmarva will supply the full requirements service that follows the Inc Load above that level. If, on any subsequent day, the Capacity PLC is less than or equal to the Base PLC plus 5 MW, the Inc Load will be turned off, and the Seller will again be obligated to provide the full requirements service that follows load up to five (5) megawatts above the Base PLC Per Bid Block.

c) Each Seller's Base PLC Per Bid Block for FP-SOS supply to MGS-S, LGS-S and GS-P customers shall be reduced during the term of the FSA under the following circumstances: If on any Business Day when the PLC Per Bid Block is equal to or less than the Base PLC Per Bid Block minus three (3) megawatts, a new Base PLC Per Bid Block shall be established which shall be equal to the Base PLC Per Bid Block in effect on the day prior to such event, minus three (3) megawatts for each whole multiple of three (3) megawatts that the PLC Per Bid Block is below the prior day Base PLC Per Bid Block. Such new Base PLC Per Bid Block shall replace the prior Base PLC Per Bid Block from the date of such adjustment forward. The intent of this provision is as follows: To the extent that 3 or more MW of PLC Per Bid Block within any of the MGS-S, LGS-S or GS-P classes switch to a competitive retail supplier, the Seller's present and future obligation to provide supply to Delmarva for its FP-SOS to such customer class is correspondingly reduced and, thus, the Seller can, but is not required to, unwind any hedges or commitments that it may deem to be in excess of its present and future obligations.

***23** d) Any Inc. load for MGS-S, LGS-S and GS-P customers shall be supplied by Delmarva and obtained through PJM. The energy shall be procured at Delmarva's zonal average LMP. Capacity shall be obtained through PJM's short-term capacity markets, short-term bilateral contracts, or at the PJM capacity deficiency rate, or through any substitute capacity construct implemented by PJM. Ancillary services costs will be as charged by PJM. A millage amount per kwh equal to that applied to the same type of customer taking FP-SOS will also be charged. The differences in costs relative to the Full Requirements Cost component of rates will be recorded and tracked in a deferral account that will be returned or recovered through the annual adjustment to the Full Requirements cost component mechanism described in section G. 1. b) above; provided, however, if the accumulated differences exceed 5% of the monthly Full Requirements Costs, then the Company may make an early filing to adjust rates prior to the beginning of the next Year.

e) The reasonable costs of administering this volumetric risk mitigation mechanism shall be recoverable in the rates charged to MGS-S, LGS-S and GS-P customers taking FP-SOS as part of the RARM component.

f) As more specifically described in the form of FSA, if a winning bidder subsequently defaults on its obligations, non-defaulting signatories to an FSA will be offered the opportunity to assume such obligations. If such obligations are assumed, the obligations of the assuming signatory will be adjusted accordingly.

I. Reports and Information Regarding Bidding and Bid Results

In addition to any restrictions that may be set forth in a confidentiality agreement, information concerning the outcome of the supply procurement may be released by the Company, DPA, Staff, and the Commission subject to the following restrictions and in the following manner:

1. All customers eligible for FP-SOS will be informed of the retail prices and the price to compare for the service for Year 1 at least two (2) months prior to the beginning of that Year. If it is not practicable to provide such notice, Delmarva shall file with the Commission and serve upon the Settling Parties notice of that fact, the reasons for the delay, and the expected date for the provision of such information. For each Year thereafter, the customers will be notified of the retail prices and price to compare as they are notified of any other rate change, *i.e.* in bill inserts within 60 days of the rate going into effect.

2. Any report concerning each year's supply procurement is not to be released until at least one month after the completion of bidding for the last tranche of that year's procurement cycle for Delmarva. Such report may list all the wholesale suppliers who were awarded supply contracts, but would not list individual bid prices or quantities. This list of winning wholesale suppliers will then be public information for all purposes.

3. If the Delaware Governor or a committee of the General Assembly requests that the Commission, Staff, the Company, or DPA release the names of the individual wholesale bidders that will be providing FP-SOS, that information shall be provided with notice that the information is confidential pursuant to this Settlement, provided however that no winning individual wholesale bidder's name will be released until at least one month after the final tranche is awarded and the Commission has approved the awards for that tranche.

4. Annually, a report may be issued by either Staff or Delmarva that shows, separate from all supplier-identifying information, the winning bid prices (expressed in dollars per MWh for the contract year) for each customer grouping. This list of winning bid prices will then be public information for all purposes.

5. If the Commission so orders, after notice and a hearing at which parties opposing release will be allowed to state the reasons for their opposition, a list which matches winning wholesale suppliers' names with their winning bid prices may be made public.

6. Any information about the supply procurement results that does not identify individual wholesale bidders, provide supplier-specific information, or disclose any individual bid prices may be made public, after all tranches of bidding for that year of FP-SOS service are completed, by the Staff, the Commission, or DPA at their discretion. Examples of such information that can be released include, but are not limited to, the total number of bids submitted, or the range in price between the lowest and the highest bids submitted.

7. In the event that a FSA with a wholesale supplier is terminated, the Company, Staff, DPA, and/or the Commission may opt to disclose any confidential information previously provided by that supplier with respect to the terminated FSA. Any information so disclosed will no longer be treated as confidential pursuant to this Settlement.

8. To the extent any information regarding the names of winning bidders, quantities purchased, or prices paid is required by law or regulation to be provided on a non-confidential basis to a federal or state regulatory agency, including but not limited to FERC Form 1 reports or SEC reports, then such disclosure shall not be deemed to violate this Settlement.

III. MISCELLANEOUS

A. Delmarva shall provide Staff and the DPA monthly data by customer class showing number of customers and quantities (by peak load obligation) served by competitive retail suppliers in the aggregate. Staff shall, within a reasonable amount of time, post the data on the Commission's web page.

B. The Commission, or if Staff requests, the Company, will procure independent consultants, paid by the Company, who will be responsible for monitoring all aspects of the procurement of the FP-SOS services described in this Settlement.

***24** 1. These consultants will be selected by, will take their direction from, and will provide their consultation and work products to, the Commission or its Staff.

2. These consultant costs will be included in the incremental costs that Delmarva will recover through the RARM described in the Settlement.

3. The consultants will provide the Commission with a final report as to each supply procurement and award. Copies of each report with appropriate redactions will be forwarded to each Party who executes a confidentiality agreement approved by the Commission.

C. Provisions in this settlement that tie a return, a carrying cost, or interest to the overall return authorized in Delmarva's next distribution base rate case, shall be read to be modified to reflect any changes in overall return authorized in any subsequent distribution base rate proceeding that becomes effective while this Settlement is still in effect.

D. The FSA shall assign to the wholesale suppliers the responsibility to obtain and assume the risk and expenses of compliance of federal and state statutory or regulatory requirements that may be imposed with respect to renewable portfolio standards, green power initiatives, distributed generation, or new load control programs.

E. If at any time while FP-SOS, HPS, or 'Inc' supply is being provided by Delmarva, any additional price or cost elements beyond those specifically addressed in this Settlement that are directly related to that service and would be incurred by Delmarva, then Delmarva may file a request with the Commission (with notice to all the Parties) for approval of recovery of those costs and, to the extent the costs are found to arise from provision of the service and are approved by the Commission, the costs will thereafter be included in the service price.

F. Notwithstanding any other provision of this Settlement, Delmarva may at any time request Commission approval to make changes in the non-price terms and conditions of its tariffs.

IV. RESERVATIONS

A. This Settlement represents a compromise for the purposes of settlement and shall not be regarded as a precedent with respect to any ratemaking or any other principle in any future case. No Settling Party necessarily agrees or disagrees with the treatment of any particular item, any procedure followed, or the resolution of any particular issue in agreeing to this Settlement other than as specified herein, except that the Settling Parties agree that the resolution of the issues herein, taken as a whole, results in just and reasonable rates, that the disposition of all other matters set forth in the Settlement are in the public convenience, necessity and interest and that, with the disposition of all such matters as set forth herein, this proceeding should be terminated with an order approving the Settlement.

B. The various provisions of the Settlement are not severable. None of the provisions shall become operative unless and until the Commission issues an order approving the Settlement as to all of the terms and conditions set forth herein without modifications or conditions. The Settlement shall be subject to waiver only by the unanimous written agreement of the Settling Parties. If any portion of this Settlement is modified, conditioned, or rejected by the Commission, the Settlement shall be considered null and void and each Settling Party individually reserves the right to proceed with the filing of testimony, briefs and evidentiary hearings as contemplated in the Commission's Orders in this proceeding. If the Settlement is rendered null and void by operation of this section III.B., the Settling Parties agree to enter into good faith negotiations to reach a new settlement. Once the Settlement has become operative under the terms of this section III.B., its terms may be revised or waived only by the unanimous written agreement of the Settling Parties or a subsequent valid order of the Commission.

C. Nothing in the Settlement shall be used to abrogate any existing or future contract for competitive retail electricity supply.

D. The headings, titles and captions of the Settlement and its various sections shall have no legal import or precedential value.

E. This Settlement may be executed in any number of identical counterparts, each of which when executed and delivered shall be an original, but all such counterparts shall constitute but one and the same instrument. Delivery by any party or its respective representatives of telecopied (counterpart) signature pages shall be as binding an execution and delivery of this Settlement by such party as if the other parties had received the actual physical copy of the entire Settlement with an ink signature from such party.

V. CONCLUSION

*25 IN WITNESS WHEREOF, intending to bind themselves and their successors and assigns, the undersigned parties have caused this Settlement to be signed by their duly-authorized representatives and the undersigned parties further recommend and urge the Commission to issue an order expeditiously approving this Settlement and making the requested findings and approvals set forth herein.

Randall V. Griffin Delmarva Power & Light Company Bruce H. Burcat Delaware Public Service Commission Staff G. Arthur Padmore Division of the Public Advocate Brian R. Greene Delaware Energy Users Group I. David Rosenstein Conectiv Energy Supply, Inc.

Footnotes

1 Delmarva's witness testified that the HPS is similar to MPSS, a currently-existing service classification in which Delmarva acquires the capacity and energy necessary to supply the load through short-term PJM markets rather than through the longer-term RFP process. The HPS energy price, like the MPSS energy price, is based on PJM's real time locational marginal pricing ('LMP ') delivered into the Delmarva Zone.

2 The purpose of the extra month in the initial contracts is to move from the May 1, 2006 start date for SOS in this proceeding to a PJM year, which commences June 1 of every year.

3 A VRM will be implemented for the large customer classes that receive the fixed price SOS (MGS-S, LGS-S and GS-P). This is in lieu of imposing a minimum stay requirement or a returning customer rule. It is designed to recognize that there are cost risks associated with customers departing from and then returning to fixed price SOS. To the extent that the fixed price SOS load per 50 MW block shrinks by 3 MW or more, the wholesale bidders' supply obligations will also be reduced. To the extent that the fixed price SOS load per 50 MW block increases by more than 5 MW, that incremental load will become Delmarva's responsibility to supply.

4 It is the method by which this 'allocable share' is determined that was the subject of the amendment to the Settlement Agreement. Both the original Settlement Agreement and the amendment assign the Delaware-retail share of the costs of the

billing system associated with the hourly priced service to GS-T customers and electing GS-P customers. The amendment uses a different mechanism than did the original Settlement Agreement for calculating each customer's share of those costs.

5 Although the term used to describe this SOS is 'fixed price,' the proposed settlement maintains existing seasonal and time of use rate differentials reflected in the current Commission-approved rates. Furthermore, because bids will be taken annually, the fixed rates will change every year.

6 *See also* 26 Del. C. § 1003(a): 'Customers of electric distribution companies in this state shall have the opportunity, but not the obligation, to purchase electricity from their choice of electric suppliers ....' (emphasis added).

7 As an example, Delmarva has noted that Exhibit D of the FSA contains a list of items on the monthly PJM bill items and specifies whether buyer (Delmarva) or seller is initially responsible for such charges. A new line item has recently been added by PJM and Exhibit D will therefore be modified to include this new line item.

8 *See* 26 Del. C. §§ 1001; 1006(a)(2)a.-c.; 1006(b)(2)a.-c.

9 *See* PSC Order No. 5941 (Apr. 16, 2002), Hearing Examiner's Report, App. A (Settlement) at ff B, C, D.1, *aff'd sub nom. Constellation New Energy, Inc. v. Public Service Commission*, 825 A.2d 872 (Del. Super. 2003); *see also* 26 Del. C. § 1010(a)(2).

10 *See* PSC Order No. 6490 (Oct. 19, 2004) at £ 3.

11 The affidavits of publication of notice from the *Delaware State News* and *The News Journal* are included in the record as Exhibit 1. Exhibits will be cited as 'Ex.__' and references to the hearing transcript will be cited as 'Tr.__.'

12 The parties who did not actively participate in the hearing and did not otherwise support or oppose the Proposed Settlement include Delaware Electric Cooperative, Inc., PSEG Energy Resources & Trade LLC, PEPCO Energy Services, Inc., Washington Gas Energy Services, Inc., Constellation Energy Commodity Group, Inc., Constellation New Energy, Inc., and PJM Interconnection, LLC.

13 The briefs submitted by the Settling Parties will be cited as '[party name] Br. at ___.' The Retail Marketers' brief will be cited as 'RM at __.'

14 According to Delmarva, the HPS is similar to MPSS, a currently existing optional service classification in which Delmarva acquires the capacity and energy necessary to supply the load through short-term PJM markets rather than through the longer-term RFP process. The HPS energy price, like the MPSS energy price, is based on PJM's real time locational marginal pricing ('LMP ') delivered into PJM's 'Delmarva Zone.'

15 The purpose of the extra month in the initial contracts is to move from the May 1, 2006 start date for SOS in this proceeding to a PJM year, which commences June 1 of every year.

16 A VRM will be implemented for the large customer classes that receive the fixed price SOS (*i.e.*, MGS-S, LGS-S and GS-P). This is in lieu of imposing a minimum stay requirement or a 'returning customer' rule. It is designed to recognize that there are cost risks associated with customers departing from and then returning to fixed price SOS. To the extent that the fixed price SOS load per 50 MW block shrinks by 3 MW or more, the wholesale bidders' supply obligations will also be reduced. To the extent that the fixed price SOS load per 50 MW block increases by more than 5 MW, that incremental load will become Delmarva's responsibility to supply.

17 Although the term used to describe this SOS is 'fixed price,' the proposed settlement maintains existing seasonal and time of use rate differentials reflected in the current Commission-approved rates. Furthermore, because bids will be taken annually, the fixed rates will change every year.

18 *See* 26 Del. C. § 1010(a)(2).

19 *See* 26 Del. C. § 1006(a)(2)(C).

20 In testimony (but not on brief), RESA also sought quarterly RFPs (rather than annual), which would raise the cost (and thus the price) of SOS, and which could discourage participation by wholesalers. (Tr. 401 (Schaub); Tr. 478 (Fisher).)

21 On brief, the Retail Marketers' also recommended that the Commission undertake a comprehensive review of the SOS process after one year to evaluate the competitive marketplace. (RM Br. at 20.) The other parties have not addressed this recommendation but I will note that such a quick review may discourage participation from retailers who decide to wait a year to see what changes are made at the end of the review period before entering the market.

22 *Rome v. Archer*, Del. Supr., 197 A.2d 49, 53 (1964) (holding that '[i]n determining the fairness of a settlement ... there is no requirement that opportunity be given the parties to hold a trial as to the issues. To do so would defeat the basic purpose of the settlement of litigation.'

23 *In Re Amsted Industries, Inc. Litigation*, 521 A.2d 1104 (Del. Ch. 1986).

End of Document

TAB 2

825 A.2d 872
Superior Court of Delaware,
New Castle County.

CONSTELLATION NEW ENERGY, INC. Appellant
v.
The PUBLIC SERVICE COMMISSION OF the STATE of Delaware, Delaware Electric Cooperative, Old Dominion Electric Cooperative, Delmarva Power & Light Company, and The Public Advocate for the State of Delaware Appellees.

Civ.A. No. 02A-07-007JOH.
|
Submitted: Dec. 18, 2002.
|
Argued: March 28, 2003.
|
Decided: April 25, 2003.

Electric company appealed decision of the Public Service Commission (PSC) approving settlement under the Electric Utility Restructuring Act. The Superior Court, New Castle County, Herlihy, J., held as a matter of first impression that: (1) evidence supported approval of settlement as in the public interest; (2) the PSC could approve settlement naming electric utility as the standard offer service supplier after transition period; (3) evidence supported rates and charges in settlement; and (4) evidence supported approval of settlement requiring utility to complete certain transmission construction projects.

Affirmed.

West Headnotes (15)

[1] **Electricity**
Service Areas;Competition

Proponents of settlement under the Electric Utility Restructuring Act and the Public Service Commission (PSC) did not need to demonstrate that each aspect of the settlement was supported by specific numeric analysis. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[2] **Public Utilities**
Proceedings Before Commissions

The Public Service Commission (PSC) may approve any settlement it finds to be in the public interest, regardless of whether that settlement has been agreed to by all parties. 26 Del.C. § 512.

Cases that cite this headnote

[3] **Public Utilities**
Review and Determination in General

The standard of review of Public Service Commission's (PSC) approval of settlement requires determination whether there is substantial evidence to support the approval of the settlement as being in the public interest and whether there is an error of law; the statute encouraging settlements does not change the applicable standard of review of PSC decisions, even those involving settlements and does not change the obligation of the PSC to have substantial evidence supporting its public interest determination. 26 Del.C. §§ 510, 512; 29 Del.C. § 10142(d).

Cases that cite this headnote

[4] **Electricity**
Service Areas;Competition

Substantial evidence concerning settlement with electric distribution company under the Electric Utility Restructuring Act supported Public Service Commission's (PSC) approval of settlement as in the public interest; company agreed to freeze its unregulated supply rates for another three years after the end of the transition period, and several experts discussed how the settlement would increase the shopping credit for commercial and industrial consumers. 26 Del.C. §§ 512, 1001 et seq.

1 Cases that cite this headnote

[5] **Electricity**

Service Areas;Competition

Settlement with electric distribution company under the Electric Utility Restructuring Act cannot be in the public interest if it offends the very statute, the Electric Utility Restructuring Act, it purports to implement. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[6] **Electricity**

Service Areas;Competition

Public Service Commission's (PSC) approval of settlement increasing standard offer service rates was supported by substantial evidence, even though the PSC did not rely on any quantitative analysis as to market prices and did not identify any numerical evidence of the regional wholesale market price; several parties to the settlement pointed out the lack of a single representative wholesale price because any such wholesale price was necessarily a composite of the prices of capacity, energy, and ancillary service.

Cases that cite this headnote

[7] **Electricity**

Service Areas;Competition

The fact that the statistical evidence and propriety models that the experts relied upon in reaching their conclusions was not admitted into evidence did not effect experts' ability to testify as to the reasonableness of the proposed electricity rates approved in settlement under Electric Utility Restructuring Act. 26 Del.C. § 1001 et seq.; Rules of Evid., Rule 703.

Cases that cite this headnote

[8] **Electricity**

Service Areas;Competition

A fixed price for an extended period of time, approximately three years under the settlement, was not contrary to purpose of the Electric Utility Restructuring Act; while the Act envisions that rates be adjusted from time to time, three years was not an inordinately lengthy period to have rates fixed. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[9] **Electricity**

Service Areas;Competition

Testimony of Public Advocate's witness about promotion of competition as result of modification of electric utility's retail tariff for large returning industrial customers was substantial evidence that settlement under Electric Utility Restructuring Act was in the public interest; the settlement allowed these customers to switch supplier's on one month's notice.

Cases that cite this headnote

[10] **Electricity**

Service Areas;Competition

Public Service Commission (PSC) could approve settlement naming electric utility, the former exclusive provider, as the standard offer service supplier after transition period under the Electric Utility Restructuring Act; the PSC had discretion and faced a relative lack of feasible alternatives. 26 Del.C. § 1010(a)(2).

Cases that cite this headnote

[11] **Electricity**

Service Areas;Competition

Public Service Commission (PSC) has discretion in choosing the standard offer service provider after transition period under the Electric Utility Restructuring Act, may setup a bidding process, or may require utility to continue to be the standard offer service supplier; the legislature's only true command is that the PSC base its decision on price, reliability, and overall quality of the electric supply service offered. 26 Del.C. § 1010(a)(2).

Cases that cite this headnote

[12] **Electricity**
Service Areas;Competition

Substantial evidence supported rates and charges in settlement under the Electric Utility Restructuring Act; the proposed increase in overall rates was generally below one percent. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[13] **Electricity**
Service Areas;Competition

Substantial evidence supported Public Service Commission's (PSC) approval of settlement requiring electric utility to complete certain transmission construction projects and undertake analyses of the economic impact of the congestion and the alleviation thereof by the construction projects; several witnesses, while admitting that the settlement's transmission congestion alleviation provisions would not eliminate all existing congestion problems, nonetheless testified that the transmission improvements required by the settlements would alleviate the congestion problem and therefore would benefit third-party suppliers and would be in the public interest under the Electric Utility Restructuring Act. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[14] **Electricity**
Service Areas;Competition

Argument that the "breakneck" pace of proceedings involving settlement under the Electric Utility Restructuring Act and approval by the Public Service Commission (PSC) prevented other interested parties from getting involved was rendered moot by the fact that no other parties ever expressed a wish to become involved. 26 Del.C. § 1001 et seq.

Cases that cite this headnote

[15] **Electricity**
Service Areas;Competition

Additional submissions that were not properly in the record before the Public Service Commission (PSC) could not be considered on appeal from its approval of settlement under the Electric Utility Restructuring Act; statute permitted appeal based upon the record before the Commission, not a trial de novo. 26 Del.C. §§ 510(c), 1001 et seq.

Cases that cite this headnote

*874 Appeal from a Decision of the Public Service Commission-**AFFIRME D.**

Attorneys and Law Firms

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G. Arthur Padmore, of Wilmington, for Public Advocate for the State of DE.

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MEMORANDUM OPINION

HERLIHY, Judge.

[1] Constellation New Energy, Inc.[1] challenges the Public Service Commission's approval of a comprehensive settlement addressing many issues with regard to Delaware's emerging competitive electric market, including the selection of rates, a standard

offer service supplier, and congestion alleviation projects. Constellation maintains that the onus is on the settlement's proponents and on the Commission to demonstrate that each aspect of the settlement is supported by specific numeric analysis, and that since no such detailed evidence has been proffered, the settlement must be rejected as not being supported by "substantial evidence." This Court disagrees and affirms the Commission's order approving the settlement. This case involves judicial review for the first time of a statute authorizing settlements of disputes before the Commission. That statute authorizes the Commission to approve settlements, even ones contested by non-settling parties, where the Commission finds such resolution to be in the public interest. Upon review of the record, there is ample evidence supporting the Commission's finding that the settlement is in the public interest. Accordingly, the Commission's order approving the settlement is **AFFIRMED**.

Facts

Prior to the enactment of the Electric Utility Restructuring Act of 1999,[2] Delmarva ***875** Power & Light Co. was the exclusive provider of retail electric service to its service territories. That regulated retail service included the generation, supply and sale of electricity, as well as the transmission and distribution of that electricity to customers. The 1999 Act altered the system by deregulating the generation, supply and sale of electricity and implementing a system based on retail competition.[3] Now, customers of electric distribution companies, such as Delmarva, have the opportunity to choose their electric supplier in a competitive marketplace. However, the Commission continues to regulate the distribution of electricity by the local utility, including rates for that service.

In the case of Delmarva, the Act provided for implementation of competition over a three-year transition period ending September 30, 2002.[4] During the transition period, Delmarva continued to supply electricity to those customers not electing another supplier, pursuant to a rate established by the Commission.[5]

In addition, the Act provides for the selection of a "standard offer service supplier." A standard offer service supplier is defined as "an electric supplier that provides standard offer service to customers within an electric distribution company's service territory after the transition period."[6] "Standard offer service" is defined as "the provision of electric supply service after the transition period by a standard offer service supplier to customers who do not otherwise receive electric supply service from an electric supplier."[7] The Commission is authorized to determine the standard offer service supplier based upon "various factors including but not limited to price, reliability and overall quality of the electric supply service offered."[8] In addition, the Commission is authorized to, in its discretion, establish a "bidding process" to determine the standard offer service supplier.[9]

Moreover, the Act authorizes the Commission to establish rules and charges with respect to customers who leave standard offer service and later return, including the "appropriate retail market price, which may be higher that the standard offer price."[10] The purpose for this provision is to allow the Commission to create a disincentive to seasonal switching. The concern is that a sophisticated customer could abuse the system by selecting a fixed rate during the high cost periods and then leave the fixed rate during low cost periods. This switching would result in a supplier serving a returning customer during high cost periods based upon rates developed from annual average costs.

On May 11, 2001, Delmarva Power & Light Company, Potomac Electric Power Company, Conectiv Communications, Inc. and New RC, Inc. filed an application with the Public Service Commission of Delaware seeking permission pursuant to 26 *Del. C.* §§ 215 and 1016 to transfer indirect control of Delmarva and Conectiv to New RC and Potomac. The Commission assigned the matter to a Hearing Examiner to conduct hearings on the application. The Commission set June 18, 2001, as the date for the initial pre-hearing and public ***876** conference and ordered newspaper publication of a notice.

A procedural schedule was approved on June 18, 2001. Public comment sessions were held on September 10, 12, and 18, 2001. Thereafter, the Public Advocate exercised its statutory right to intervene. In addition, several other

interested parties sought and were granted leave to intervene in the proceedings. These parties include the International Brotherhood of Electrical Workers Local Union 1307, BOC Gases, Inc., Consumers Education & Protective Association of Delaware, Mr. Bernard J. August, Cable Telecommunications Association of MD, DE & DC, Old Dominion Electric Cooperative, the Delaware Electric Cooperative, the Delaware Energy Users Group and AES NewEnergy, Inc. (the appellant). Old Dominion Electric Cooperative and the Delaware Electric Cooperative will herein be referred to collectively as the "Cooperatives."

An evidentiary hearing was conducted on November 28, 2001, at which time the parties informed the Hearing Examiner that they were in the middle of informal settlement negotiations and near to reaching an agreement. There was an array of competing interests involved; these parties are certainly not traditional allies. Some parties, such as the cooperatives, apparently focused on relieving congestion, while others, like Delmarva and the Public Advocate, were more concerned about setting appropriate rates. Nevertheless, later that day, the parties reached an agreement. Constellation, the sole objector, noted its objections to the proposed settlement and was granted leave to file written testimony in opposition to it. Interestingly, several provisions of the settlement were included at the request of Constellation, the settlement's sole objector. A hearing to receive evidence and testimony was scheduled for December 18, 2001, and public notice was published in the Delaware State News and the News Journal. The relevant portions of the notice stated:

> On May 11, 2001, Delmarva Power & Light Company ("Delmarva"), Conectiv Communications, Inc. ("CCI"), Potomac Electric Power Company ("Pepco") and New RC, Inc. ("New RC") (together, "Applicants") filed an Application and testimony with the Delaware Public Service Commission ("Commission") seeking approval of a merger and related transactions (the "Merger") as described by Applicants. (1) Conectiv, the parent company of Delmarva and CCI, would merge with a subsidiary of New RC, with Conectiv as the surviving corporation; and (2) Pepco would merge with a different subsidiary of New RC, with Pepco as the surviving corporation; and (3), consequently, New RC would become the parent company of Pepco and Conectiv, with Conectiv continuing to own Delmarva and CCI.
>
> * * * * * *
>
> The proposed settlement executed by the Applicants and some of the other parties to the proceeding would approve the proposed merger subject to a number of conditions, including: 1) delivery and supply rate changes, 2) default supply service obligations, 3) commitments regarding corporate activities, 4) investments and contributions in Delaware, 5) transmission reliability and congestion issues, 6) merger costs, 7) service level guarantees, 8) certain competitive supplier issues, and 9) a removal of the Rate Q service classification from the tariff.

The settling parties filed the proposed settlement, supported by all parties except Constellation, on November 30, 2001. Some highlights from the proposed settlement include:

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- ☐ Delmarva will remain the standard offer service ("SOS") supplier from May 1, 2003, through May 1, 2006, and the applicable rates for SOS's supply service will be representative of the regional wholesale electric market price plus a reasonable allowance for retail margin.

- ☐ For the period beginning on October 1, 2002, and ending on September 1, 2003, Delmarva will amend its tariff on returning customers such that an industrial or commercial customer returning to Delmarva's Standard offer service will pay either the Market Priced Supply Service ("MPSS") or a negotiated market price.

- ☐ For the period beginning on October 1, 2002, and ending on September 30, 2003, Delmarva will shift the Competitive Transition Charge ("CTC") rates for commercial and industrial customers [11] from the delivery component of rates to the supply (or unregulated) component.

- ☐ For the period beginning on October 1, 2002, and ending on September 30, 2003, Delmarva will shift the nuclear decommissioning costs for commercial and industrial customers [12] from the delivery component of rates to the supply component.

☐ For the period beginning on October 1, 2003, until May 1, 2006, Delmarva will increase the supply components of rates for commercial and industrial customers[13] by 103% of the prior rates, less the decommissioning costs.

☐ Effective October 1, 2003, until May 1, 2006, Delmarva will increase the delivery component of rates for residential and SGS-ND customers by 3%, and reduce rates to reflect the removal of decommissioning costs.

☐ Effective October 1, 2003 until May 1, 2006, rates will be frozen except that Delmarva will be permitted to seek: (i) recovery of extraordinary costs pursuant to 26 *Del. C.* § 1006; (ii) via a one-time recovery in the transmission component of rates, the cost of FERC-approved rate changes; (iii) a one-time recovery of changes in ancillary charges billed by PJM; (iv) to change certain optional services; (v) to change its rate design if such change is revenue neutral to Delmarva and among its customer classes; (vi) to change its rules and regulations; (vii) to change the credits for load management programs; and (viii) to change the MPSS rate to more accurately reflect market costs.

☐ Delmarva and BOC will terminate with prejudice the litigation in Docket No. 00-653 and enter into a special interim contract.

☐ Delmarva will agree with its two existing Rate Q customers on a process to move them to different contracts and to terminate Rate Q service on or about November 2, 2002.

☐ For the next 5 years, Delmarva's operational headquarters and significant senior management will remain in Delaware.

☐ For the next 6 years, Delmarva's charitable contributions will be maintained at levels comparable to its historic levels.

☐ Applicants will contribute $750,000 to Murex Investments so as to trigger *878 matching state or federal funds, on the condition that the funds are spent on job training and small business development in Delmarva's Delaware service territory.

☐ Delmarva will not seek rate recovery of the merger transaction costs or the merger acquisition premium, including the break up fee if the merger does not occur.

☐ Delmarva will contribute $200,000 to an organization designated by Staff and DPA to promote renewable resources in Delaware and will assist in informing customers of such organization.

☐ Delmarva will participate in a working group to identify and develop cost-effective demand side management or conservation programs.

☐ Delmarva will implement a small pilot program for residential and small commercial consumers to test real-time metering or similar technologies.

☐ Delmarva will adopt the "appointments kept," "new residential customer installations," "bill accuracy" and "outage restorations" Service Level Guarantees with certain modifications, and the remaining proposed service level guarantees will be addressed in separate proceedings.

☐ Delmarva will modify its tariff provisions to benefit competitive electric suppliers with respect to the availability of electronic data.

☐ Delmarva will undertake to develop and implement within 9 months post-merger a "web-based mechanism" to transfer customers' historic interval data to competitive suppliers.

☐ Three transmission projects to be completed by May 2008 will be added and one currently scheduled transmission project will be accelerated.

☐ Delmarva will implement a methodology designed to reduce congestion on its transmission system using analysis of "off-cost operations" data available from PJM.

☐ Pursuant to 26 *Del. C.* § 1006(a)(2), Delmarva will file schedules demonstrating its overall return based upon cost of service data on or before March 30, 2002.

☐ On or before September 1, 2005, Delmarva will file a class cost of service study to permit a review and determination of the justness and reasonableness of its regulated rates on or after May 1, 2006.

☐ Each settling party may petition the Commission to reopen the record within 30 days of the filing of a Maryland settlement in Applicants' merger filing in that state.

During the December 18, 2001, public hearing, Constellation presented supplementary testimony in opposition to the settlement and the other parties presented testimony in support of it. A public comment session was conducted on December 20, 2001. In February, 2002, after the parties submitted briefing in support of their positions, the Hearing Examiner issued his report which recommended that the Commission approve the proposed settlement.

The Commission heard oral argument on March 19, 2002. On April 16, 2002, the Commission adopted the Examiner's findings and recommendation. Constellation filed a Petition for Rehearing and Reconsideration, which was denied on June 4, 2002. Thereafter, Constellation appealed the Commission's decision to this Court. Constellation makes several arguments on appeal.

First, Constellation maintains that the Commission's approval of increased standard offer service rates was arbitrary and ***879** unsupported by substantial evidence. Title 26, section 1006(a)(1)a. of the Delaware Code provides that the retail market price for electric supply service for the transition period shall be "based upon and/or representative of regional wholesale electric market prices, plus a reasonable allowance for retail margin." Section 1006(a)(2)a. provides that at the end of the transition period, the retail market price under subparagraph (a)(1)a. shall become the standard offer service price. Constellation faults the Commission because it did not rely on any qualitative analysis as to market prices. Essentially, it maintains that the Commission did not identify any numerical evidence of the "regional wholesale market price" or "reasonable allowance for retail margin," thereby depriving this Court of the ability to determine that its decision was based on substantial evidence. Constellation also makes other tangential arguments. For instance, it argues that a fixed price for an extended period of time-approximately three years under the settlement-is contrary to the Electric Utility Restructuring Acts's purpose. Also, Constellation rejects the Commission's reasoning that 26 *Del. C.* 512, which directs the Commission to approve stipulations and settlements that it finds to be "in the public interest," eliminates the need for other considerations. According to Constellation, the Commission is relying on section 512 to avoid its statutory ratemaking obligations and responsibility to implement retail competition in the state. In short, Constellation accuses the Commission of simply choosing to ignore the absence of evidence and lay blame upon Constellation for failing to supply its own, thereby improperly shifting the burden from the settling parties to the objecting party.

Second, Constellation contends that the Commission's extension of the standard offer service obligation of Delmarva is unsupported by substantial evidence. Pursuant to the settlement, Delmarva has been named to be the standard offer service supplier from the conclusion of the existing transition period, May 1, 2003, through May 1, 2006. Constellation maintains that there was no evidentiary basis for this decision and that it is arbitrary and capricious. By statute,[14] it argues, the Commission must consider the "price, reliability and overall quality of electric service"[15] of potential suppliers in determining the standard offer service supplier following the transition period. Since the Commission only considered these factors in a cursory manner, the argument continues, the Commission's decision is erroneous as a matter of law.

Third, Constellation maintains that the distribution rates and charges approved by the Commission are arbitrary and unsupported by substantial evidence and therefore erroneous as a matter of law. The settlement, in addition to establishing new standard offer service rates, provides for new adjusted distribution rates for Delmarva. The thrust of Constellation's complaint is that the Commission appears to have put significant emphasis on the fact that the rates were the product of "extensive negotiations", rather than undertaking an extensive statistical analysis. Constellation states, "Having been deprived of an evidentiary basis upon which to determine the appropriateness, justness and

reasonableness of the rates, the settling parties are simply asking the Commission to accept the product of their self-interested negotiations." [16]

*880 Fourth, Constellation characterizes the Commission's decision regarding service congestion cost mitigation as being arbitrary and capricious, unduly preferential with regard to certain customers, and unsupported by substantial evidence. Under the approved settlement, Delmarva will complete certain transmission construction projects and will be required to undertake analyses of the economic impact of the congestion and the alleviation thereof by the construction projects. Constellation opposed these various mechanisms, arguing that while these proposals may assist Delmarva in reducing its own congestion related supply costs, the mechanisms do nothing to address congestion related costs that are incurred by competing energy suppliers. Constellation maintains that these measures do nothing to facilitate competition and are discriminatory, thus resulting in unjustly discriminatory rates in violation of 26 *Del. C.* §§ 303 and 311.

Fifth, Constellation argues that the notices for the underlying proceeding provided inadequate notice to interested parties of the Commission's intention to resolve issues unrelated to the proposed merger. It maintains that the limited efforts of the Commission to provide public notice to affected parties were deficient insofar as they failed to adequately describe the actual nature of the proceedings. Constellation likens the notices to "laundry lists" which contain information about the proceedings, but which bury the information among technical minutia. As a result, Constellation maintains, it was the one isolated opponent of the settlement.

Lastly, Constellation contends that the Commission based its decision on erroneous and misleading evidence that renders its orders erroneous as a matter of law. In advancing this argument, Constellation proffers comments made by the settlement's proponents in various proceedings in different states. These comments are of significant relevance, it suggests, because they are at odds with the positions taken before the Commission. In particular, Constellation argues that the parties have taken different positions before the different proceedings, positions that will produce different results not only for the development of the competitive market, but also the manner and role in which the applicants engage that market. In short, Constellation argues that the statements are so inconsistent that they raise the specter that parties have been disingenuous with the Commission, thereby calling into question the integrity of the Commission's decision.

Standard of Review

Two statutes govern the scope and standard of this Court's review of the Commission's Orders. The scope of review is found in 26 *Del. C.* § 510, as follows:

> (b) The appeal shall not be a trial de novo but shall be based upon the record before the Commission.
>
> (c) The scope of review before the Court shall be that the Commission's findings shall be upheld if they are supported by sufficient evidence, free of error of law and not arbitrary or capricious. When factual issues are reviewed the Court shall take due account of the presumption of official regularity and quasi-legislative function and specialized competence of the Commission. [17]

29 *Del. C.* § 10142(d) sets forth the appropriate standard of review:

> The Court's review, in the absence of actual fraud, shall be limited to a determination of whether the agency's decision *881 was supported by substantial evidence on the record before the agency. [18]

Furthermore, this Court sits as a "reviewing court, not as an administrative agency of superior rank." [19]

Discussion

I.

While Constellation alleges six grounds for appealing the Commission's order approving the settlement, much of its argument is premised on the implicit proposition that the Commission's approval of the settlement turned this case into a traditional rate case. Therefore, according

to Constellation, substantial evidence in support of the Commission's approval of the adjustments to the supply and delivery components of the rates is required and the Applicants have the burden of proving the reasonableness of the rates.

Constellation relies heavily on *Application of Wilmington Suburban Water Corp.* [20] for the following proposition:

> All utility rate cases are subject to an overriding public interest, since the Commission must regulate the rates chargeable by a legalized monopoly. The general public must ultimately sustain the burden of the rates. Thus, the Commission, as an administrative agency, represents the state and the public in all matters properly before it. It stands between the public and the utilities. Before a commission [sic] makes a finding upon an ultimate issue of fact, public policy requires that the public interest be protected either by a full hearing on all the evidence relating to that issue of fact or that the basis of the Commission's findings clearly appear in the record. [21]

From this backdrop, Constellation instructs, "In a matter such as this, this Court in its review process must clearly apply, in addition to those requirements of statute establishing the parameters of its review, the guidance of the *Wilmington Suburban Water* analysis." [22] In that case, the Supreme Court, among other things, reproached the Commission for its "unwise" decision to enter into a stipulation which could be construed or argued as a stipulation on an ultimate issue of fact. [23]

[2] While the cases Constellation cites are certainly of significant historical importance, Constellation's reliance on them is misplaced because in the many years that have past since they were decided, the Delaware regulatory system has changed. Most importantly for the purposes of this discussion, 26 *Del. C.* § 512 was enacted. Prior to that enactment, the Commission did not have the authority to approve settlements or to permit the parties to stipulate to facts, so essentially every proceeding brought before the Commission was litigated to conclusion. The new statute, entitled "Settlements are to be encouraged", provides:

> (a) Insofar as practicable, the Commission shall encourage the resolution of matters brought before it through the use of stipulations and settlements.
>
> (b) The Commission's staff may be an active participant in the resolution of such matters.
>
> (c) The Commission may upon hearing approve the resolution of matters *882 brought before it by stipulations or settlements whether or not such stipulations or settlements are agreed to or approved by all parties where the Commission finds such resolutions to be in the public interest. [24]

In other words, the legislature has determined that settlements are to be encouraged and that the Commission may approve any settlement it finds to be in the public interest, regardless of whether that settlement has been agreed to by all parties. It is important to note that no court has yet had the opportunity to apply this provision since its enactment in 1995; thus, this case deals with an issue of first impression.

[3] Even with this new statute, the normal standards of appellate review, enunciated earlier, still apply. In other words, is there substantial evidence to support the Commission's approval of the settlement as being in the public interest and/or did it commit an error of law? The Court concurs with Constellation that section 512 does not change the applicable standard of review of Commission decisions, even those involving settlements. Nor does the statute change the obligation of the Commission to have substantial evidence supporting its public interest determination.

[4] Generally speaking, there is ample substantial evidence from which the Commission could conclude the settlement to be in the public interest. First of all, as part of the settlement, Delmarva agreed to freeze its unregulated supply rates, over which the Commission has no authority, for another three years after the end of the transition period. The Commission heard testimony of Andrea Crane, the Public Advocate's expert witness, who testified that the rate certainty of the frozen rates is a benefit in and of itself, regardless of the level of the rates:

> Q: (Hearing Examiner): In your oral testimony you indicated that you considered the rate certainty aspect of the proposed settlement to be a great benefit to consumers. Would this only apply if the proposed settlement rates are below market rates throughout the term of the proposed settlement's rates?

> A: (Ms. Crane): No, I think rate certainty is a benefit regardless of the rate level. I mean, a customer may be willing today to lock in a certainty rate for a long-term period even if there's a possibility that rates will fall in the future. It's essentially like an insurance policy; you know what you'll be paying. And I think there is a benefit to that even if I may not get the very, very lowest rate possible during this four or five year period, at least I know what my costs are going to be, and I think there's a benefit to that. [25]

Additionally, several experts discussed how the settlement will increase the shopping credit for commercial and industrial consumers. [26] A shopping credit is the rate or price per electric unit used for comparing one energy supplier against another in a competitive retail environment. The rate generally reflects the price, expressed in kilo watt hours, to a customer for the supply portion of his or her bill. In order for an alternate energy provider to be competitive, wholesale electricity must be purchased and sold to retail customers at a price lower than the shopping credit. Therefore, increasing the shopping credit ***883** enhances the ability of alternate suppliers to compete for retail customers in Delaware. And the largest increases in the shopping credits are for the larger customer classes, those most likely to embrace alternate electric suppliers.

There is evidence of other benefits to Delaware that the Commission could rely upon in approving the settlement, but the Court need not belabor them here. [27] The Court also notes that it puts significant weight on the opinion of the Public Advocate, a party charged by statute [28] to protect the Delaware ratepayers, that the settlement is in Delaware's best interest.

[5] However, Constellation is correct insofar as it maintains that the settlement cannot be in the public interest if it offends the very statute, the Electric Utility Restructuring Act, it purports to implement. Accordingly, the Court will address each of Constellation's specific arguments in turn.

II.

[6] Constellation's first argument is that the Commission's approval of increased standard offer service rates was arbitrary and unsupported by substantial evidence. Title 26, section 1006(a)(1)a. of the Delaware Code provides:

> The retail market price for electric supply service (including losses to the customer's delivery point) shall be estimated and applied separately for each customer rate class for each year of the transition period. Such prices shall be based upon and/or representative of regional wholesale electric market prices, plus a reasonable allowance for retail margin to be determined by the Commission. Once established, such prices shall not thereafter be changed by the Commission during the transition period, except as the result of an appeal of the Commission's decision. [29]

In addition, section 1006(a)(2), labeled "Rates in effect after the transition period", provides in part:

> a. At the end of the transition period set forth in § 1004(a) of this title, the retail market price under subparagraph (a)(1)a. of this section shall become the standard offer service price.
>
> b. Such standard offer service price shall be the applicable retail market price for electric supply service for any customers who have not chosen an alternate electric supplier or have returned to obtaining their electric supply service from the standard offer service supplier, subject to such regulations as the Commission may adopt pursuant to § 1010(c) of this title for returning customers.
>
> c. If DP & L is a standard offer service supplier, the standard offer service price ***884** shall be revised by DP & L from time to time for each customer rate class to be representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin to be determined by the Commission for providing such electric supply service. The standard offer service price may be reviewed from time to time by the Commission to determine whether it represents

> the regional wholesale electric market price, plus a reasonable allowance for retail margin. [30]

Constellation criticizes the Commission because it did not rely on any quantitative analysis as to market prices. Essentially, it maintains that the Commission did not identify any numerical evidence of the "regional wholesale market price," or "reasonable allowances for retail margin." Constellation concludes that since the Court cannot identify-and therefore cannot review-the components of the price determination formula setup under section 1006, the Court cannot find that the Commission's decision was based on substantial evidence.

Constellation's argument that the Commission lacked analytical data upon which to base its decision was echoed by its expert witness, Edward Toppi. While some of his testimony appeared to opine that the proposed rates were too low, Toppi clarified his position:

> Q: Let me ask you a question based on the nature of your testimony, Mr. Toppi. Am I correct to understand in reviewing this testimony and primarily the rebuttal testimony marked as Exhibit 16 that AES's major complaint is that the proposed rates are too low?
>
> A: No. That is not a correct statement.
>
> Q: Other than the process by which the rates have been proposed in the settlement, what other major complaint does AES have with the establishment of the rates?
>
> A: Other than the process by which they were arrived at?
>
> Q: Correct.
>
> A: None.
>
> Q: None? I'm sorry. I didn't hear you.
>
> A: That's correct. None.
>
> Q: So the results from AES's perspective is satisfactory. It's the process that you have a problem with?
>
> A: I can't make, you know, a statement about the results, because the-our belief is that the process to arrive at the results essentially did not take into account all the elements that it should have and, therefore, the results are-I don't know if they're good, bad, right on. It takes time to-I don't think the time and the process to which they were established was adequate to make that determination. [31]

However, several parties to the settlement and appellees point out that there is no single "wholesale price" that can be said to be "representative." This is because any such wholesale price is necessarily a composite of the prices of capacity, energy, and ancillary service, each of which will vary depending on whether one looks at today's prices, future price curves generated by models, or bid and ask prices in futures markets. Additionally, all of these factors are necessarily evaluated by each market participant through the lens of its perceptions of the risks assumed for variations in weather, customer usage, risks of lost or added customers, and other forces. Therefore, they conclude, any determination as to whether a particular ***885** standard offer service price is representative of regional wholesale market price plus a reasonable allowance for retail margin necessarily entails judgements not easily reducible to a mathematical formula. That is why, the argument continues, it was necessary for the Commission to take the "end results" approach, relying on the experts' opinions that the settlement's rates were reasonable approximations.

Delmarva's expert, Joseph Wathen, testified that the standard offer service prices reflected in the settlement are representative of the wholesale market in that the rates are high enough to recover wholesale costs plus a margin. [32] His opinion was based on an evaluation using proprietary tools of Delmarva. Additionally, Commission Staff witness Janis Dillard testified that the proposed prices were representative of wholesale market prices plus a reasonable margin based upon an analysis of historic data. More specifically, Dillard testified:

> A. Well, when we started into this settlement process I did try to do an analysis and it was based on historic data. It wasn't forward looking. But what I tried to look at were two things: I tried to look at the contracts that Delmarva had in place and I looked at the price of those, and then I also took a look what I'll call the incremental cost of power [as reported by the PJM Interconnection, LLC, or simply "PJM"]. And what I did was an analysis where I took an energy price that was based on the DP & L locational marginal price for a 13-month period for every hour of a 13-month, and I compared that to an hourly load profile. So I figured what the energy cost

would be if a customer had to buy in PJM real-time market. I added in a component for typical mark-up for a supplier. I believe it's two to five mills. So this kind of marginal rate to me represented a ceiling of what the cost would be for this 13-month period, May 2000 through May 2001. And the results were that the ceiling represented by the locational marginal price and the I-cap rate were about 5.134 to 5.634 cents depending on your assumptions. And the bottom of the range I looked at which represented Delmarva's locked-in contracts represented a rate of 3.392 to 3.634. And the rates that are being proposed in the settlement fall within that range, so I felt comfortable that they weren't higher than market and I felt comfortable that they weren't so low that Delmarva was going to lose money. [33]

[7] In addition, while Constellation's objection is not strictly evidentiary in nature, the Court nevertheless finds the Delaware Rules of Evidence instructive. Rule 703 provides that "[t]he facts or data ... upon which an expert bases an opinion or inference ... if of a type reasonably relied upon experts in the particular field in forming opinions or inferences upon the subject ... need not be admissible in evidence." Therefore, the fact that the statistical evidence and propriety models that the experts relied upon in reaching their conclusions was not admitted into evidence, in no way affects the expert's ability to testify as to the reasonableness of the proposed rates. Furthermore, Rule 705(b) provides for objections by adverse parties on the ground that the expert does not have a sufficient basis for expressing an opinion, in which case a voir dire examination directed to the underlying facts or data is to be conducted. In this case, both Wathen and Dillard were subject to cross-examination and yet the Commission evidently ***886** still found their testimony persuasive. Nor does it appear Constellation timely raised an objection.

[8] Constellation, however, also makes two corollary arguments. First, it asserts that a fixed price for an extended period of time-approximately three years under the settlement-is contrary to the Electric Utility Restructuring Act's purpose. The Court is not persuaded. All rates are fixed, whether they are fixed for six months or six years. Therefore, Constellation's objection, as the Court interprets it, is that it would prefer to have the rates revised more frequently than as set out in the settlement. While the Court agrees with Constellation insofar as it asserts that the Electric Utility Restructuring Act envisions that rates be adjusted from time to time, in the Court's view, three years is not an inordinately lengthy period to have rates fixed. After the period, a new rate review would be conducted. Indeed, the Delaware General Assembly clearly believed that three years is not an inappropriately long period of time to freeze rates; the Electric Utility Restructuring Act, itself, mandated that rates be frozen for a period of three years. [34]

[9] Second, Constellation maintains that the market priced supply service provision of the settlement would stifle competition and thwart development of the competitive market envisioned by the Electric Utility Restructuring Act. [35] The settlement, as approved by the Commission, modifies returning customer provisions in Delmarva's retail tariff. The larger, non-residential customers who obtain their supply from a competitive supplier and then return to Delmarva for supply service currently have a choice of pricing plans. They can choose to be served under a market priced supply service using a real-time fluctuating price published by an independent regional organization. This option allows them the freedom to switch to a competitive supplier on one month's notice. Alternatively, they can choose to be put on a fixed rate service, but in which case they would be unable to switch their supplier for twelve months. The settlement modifies the existing market priced supply service tariff and makes it mandatory. In other words, the twelve-month fixed rate option is eliminated. With regard to residential and smaller business customers, the settlement applies a twelve-month minimum stay requirement for returning customers.

The Commission, however, heard the testimony of the Public Advocate's witness, Andrea Crane, who opined that the settlement's mandatory market price supply service provision for large customers would actually promote competition. [36] These larger, more sophisticated entities, she reasoned, are well equipped to evaluate their options and the market priced supply service would only enhance their ability to pursue their best interests. Joseph Wathen testified similarly. [37]

The foregoing constitutes substantial evidence from which the Commission could ***887** conclude that approval of the settlement with the proposed rates were in the public interest.

III.

[10] Constellation next argues that the Commission's extension of the standard offer service obligation of Delmarva is unsupported by substantial evidence. Pursuant to the settlement, Delmarva has been named to be the standard offer service supplier from the conclusion of the existing transition period, May 1, 2003, through May 1, 2006. Constellation maintains that there was no evidentiary basis for this decision and that it is arbitrary and capricious. By statute,[38] it argues, the Commission must consider the "price, reliability and overall quality of electric service"[39] of potential suppliers in determining the standard offer service supplier following the transition period. Since the Commission only considered these factors in a cursory manner, the argument continues, the Commission's decision is erroneous as a matter of law.

Title 26, section 1010(a)(2) of the Delaware Code provides:

> Prior to the end of the transition period set forth in § 1004(a) of this title, the Commission shall determine who the standard offer service supplier in DP & L's service territory will be following the transition period, based on various factors including but not limited to price, reliability and overall quality of the electric service offered. In determining the standard offer service supplier for DP & L's service territory, the Commission may use an auction bidding process.... Nothing in the Commission's rules or regulations shall prohibit DP & L or its affiliates from participating in the bidding process for posttransition standard offer service. The Commission may also require DP & L to continue to be the standard offer service supplier or to supply a portion of the standard offer service after the transition period.[40]

[11] The language of section 1010 clearly indicates that the Commission has discretion in choosing the post-transition period standard offer service provider. It *may* setup a bidding process or it *may* require Delmarva to continue to be the standard offer service supplier. The legislature's only true command is that the Commission base its decision on "price, reliability and overall quality of the electric supply service offered."[41]

In reality, a standard offer service provider must have the financial and institutional capabilities to obtain reliable sources of capacity and energy and the flexibility to meet the needs of customers. It is a demanding position. According to a Commission Staff evaluation, Constellation was unwilling to consider taking the position except at levels significantly higher than the settlement provides.[42] Additionally, true competition has yet to be achieved in Delaware. In her pre-filed testimony, Andrea C. Crane explained that the number of customers buying energy from alternate suppliers peaked at 202 and has fallen to eight, one of which is residential.[43] With respect to reliability and overall quality of service offered, it is very unlikely that there is any competitive supplier that would be interested in serving Delaware ***888** and would exceed Delmarva's qualifications.

In short, in light of the discretion the Assembly has given the Commission, the relative lack of feasible alternatives, and the legislature's pronouncement that settlements are to be encouraged, this Court finds that the Commission did not err.

IV.

[12] Constellation's third argument is that the rates and charges approved by the Commission are arbitrary and unsupported by substantial evidence and therefore erroneous as a matter of law. The settlement, in addition to establishing new standard offer service rates, provides for new adjusted distribution rates for Delmarva. Constellation criticizes the Commission because it appears to have put significant emphasis on the fact that the rates were the product of "extensive negotiations," rather than undertaking an extensive statistical analysis. In particular, it asserts that the Commission's approval of the settlement "could easily place Delmarva ratepayers at future risk should it become necessary for Delmarva

to make above market energy purchases to meet its load obligations resulting in the future, deferred collection of energy costs." [44] Constellation concludes, "Having been deprived of an evidentiary basis upon which to determine the appropriateness, justness and reasonableness of the rates, the settling parties are simply asking the Commission to accept the product of their self-interested negotiations." [45]

But the Commission found that the settlement was beneficial to ratepayers because its proposed increase in overall rates was generally below one percent, ranging from and increase of about 0.3% to an increase of about 1.4%, and that the levels would be frozen until May 2006. [46] It relied on the testimony of Joseph Wathen. [47] The Commission agreed with Wathen that in return for the modest rate change, the ratepayers will enjoy a price freeze, which will promote competition. [48] Several witnesses also testified that the rates are reasonable and that Delmarva should not lose money at the settlement's rates, notwithstanding fluctuating market prices. [49]

In essence, Constellation challenges the Commission's decision to believe appellees' witnesses rather than Constellation's witness. The Court is not equipped to upset that decision.

V.

[13] Constellation next characterizes the Commission's decision regarding service congestion cost mitigation as being arbitrary and capricious, unduly preferential with regard to certain customers, and unsupported by substantial evidence. Under the approved settlement, Delmarva will complete certain transmission construction projects and will be required to undertake analyses of the economic impact of the congestion and the alleviation thereof by the construction projects. Constellation opposed these various mechanisms, arguing that while these proposals may assist Delmarva in reducing its own congestion related supply costs, the mechanisms do nothing to address congestion related costs that are incurred by competing energy suppliers. Constellation maintains ***889** that these measures do nothing to facilitate competition and are discriminatory, thus resulting in unjustly discriminatory rates in violation of 26 *Del. C.* §§ 303 and 311.

As Delmarva points out in its brief, there are two factors that affect the generation and transmission of electricity that are relevant to the congestion problem. First, there are physical limitations on the amount of electricity that can be moved from one region to another. Second, some power plants are cheaper to run than others due to fuel, location and other factors. Congestion occurs when demand is very high or when transmission or generation facilities become unavailable, for example, due to maintenance. While congestion problems could be virtually eliminated by enormously expanding the transmission system, the costs involved in such an undertaking would outweigh the possible benefits. [50]

The Commission contends that Constellation failed to raise its "discriminatory rates" argument before it and that therefore this Court need not address it. Putting that contention aside, the Court finds Constellation's claim to be without merit. Several witnesses, while admitting that the settlement's transmission congestion alleviation provisions would not eliminate all existing congestion problems, nonetheless testified that the transmission improvements required by the settlements would alleviate the congestion problem and therefore would benefit third-party suppliers and would be in the public interest. [51] In fact, John W. Rainey testified on behalf of the Cooperatives, which are very concerned with congestion problems, that the undertakings contained in the settlement will "go a long way in improving the transmission congestion problem on the Delmarva peninsula." [52] Thus, the Commission could rely on those experts' testimony in approving the settlement. Once again, an agency, as a finder of fact, may credit evidence upon which it relies to the detriment of conflicting evidence.

Furthermore, Constellation has provided no basis for its accusation that the provisions are somehow discriminatory. Instead, it merely bootstraps its argument by pointing out that there is no evidence on the record to refute its unsupported statement.

VI.

Constellation next argues that the notices for the underlying proceeding provided inadequate notice to

potential parties of the Commission's intention to resolve issues unrelated to the proposed merger. It maintains that the limited efforts of the Commission to provide public notice to affected parties were deficient insofar as they failed to adequately describe the actual nature of the proceedings. Constellation likens the notices to "laundry lists" which contain information about the proceedings, but which bury the information among technical minutia. As a result, Constellation maintains that it was the one isolated opponent of the settlement.

The Commission may decide the manner and method of giving notice to persons likely to be interested in the matter or proceeding.[53] By statute, it may order that notice be effected by various means, ***890** including by publication in one or more publications of general circulation.[54] This was the method utilized by the Commission in this case. The relevant portions of the notice stated:

> On May 11, 2001, Delmarva Power & Light Company ("Delmarva"), Conectiv Communications, Inc. ("CCI"), Potomac Electric Power Company ("Pepco") and New RC, Inc. ("New RC") (together, "Applicants") filed an Application and testimony with the Delaware Public Service Commission ("Commission") seeking approval of a merger and related transactions (the "Merger") as described by Applicants. (1) Conectiv, the parent company of Delmarva and CCI, would merge with a subsidiary of New RC, with Conectiv as the surviving corporation; and (2) Pepco would merge with a different subsidiary of New RC, with Pepco as the surviving corporation; and (3), consequently, New RC would become the parent company of Pepco and Conectiv, with Conectiv continuing to own Delmarva and CCI.
>
> * * * * * *
>
> The proposed settlement executed by the Applicants and some of the other parties to the proceeding would approve the proposed merger subject to a number of conditions, including: 1) delivery and supply rate changes, 2) default supply service obligations, 3) commitments regarding corporate activities, 4) investments and contributions in Delaware, 5) transmission reliability and congestion issues, 6) merger costs, 7) service level guarantees, 8) certain competitive supplier issues, and 9) a removal of the Rate Q service classification from the tariff.

The entire notice was less than two pages long and clearly delineated the issues to be addressed. Constellation's "laundry list" argument is unpersuasive. Additionally, the parties likely to be interested in these issues are sophisticated entities, fully capable of realizing the importance of the proceedings from the notice.

[14] Also, Constellation's argument that the "breakneck" pace of the proceedings prevented other interested parties from getting involved is mooted by the fact that no other parties ever expressed a wish to become involved. If such a party had sought to participate, it could have simply requested additional time from the Hearing Examiner. But no party came forward.

The Commission did not err with regard to public notice.

VII.

[15] Lastly, Constellation contends that the Commission based its decision on erroneous and misleading evidence that renders its orders erroneous as a matter of law. In advancing this argument, Constellation proffers comments made by the settlement's proponents in various proceedings in different states. These comments are of significant relevance, it suggests, because they are at odds with the positions taken before the Commission. Constellation maintains that the parties have taken different positions before the different proceedings, positions that will produce different results not only for the development of the competitive market, but also the manner and role in which the applicants engage that market. In brief, Constellation argues that the statements are so inconsistent that they raise the specter that parties have been disingenuous with the Commission, thereby calling into question the integrity of the Commission's decision.

Title 26, section 510(c) of the Delaware Code, however, clearly provides that an ***891** appeal shall not be a trial de novo but shall be "based upon the record before the Commission."[55] Therefore, since the additional submissions provided by Constellation was not properly in the record before the Commission, this Court declines to consider them. Constellation's argument fails accordingly.

Conclusion

For the reasons stated herein, the Public Service Commission's finding the settlement to be in the public interest and order approving the settlement was based on substantial evidence. Accordingly, the Commission's Order is **AFFIRMED.**

All Citations

825 A.2d 872

Footnotes

1 On September 9, 2002, Constellation Energy Group acquired AES NewEnergy and the entity is now known as Constellation New Energy, Inc ("Constellation").

2 Title 26, chapter 10 of the Delaware Code.

3 26 *Del. C.* 1003(a).

4 26 *Del. C.* 1004(a).

5 26 *Del. C.* §§ 1006(a)(1) a. and 1010(a).

6 26 *Del. C.* § 1001(16).

7 26 *Del. C.* § 1001(15).

8 26 *Del. C.* § 1010(a)(2).

9 *Id.*

10 26 *Del. C.* § 1010(c).

11 Excluding those receiving service under Service Classification SGS-ND.

12 Excluding those receiving service under Service Classification SGS-ND.

13 Excluding those receiving service under Service Classification SGS-ND.

14 26 *Del. C.* 1010(a)(2).

15 *Id.*

16 Appellant's Br. at 19.

17 26 *Del. C.* § 510.

18 29 *Del. C.* § 10142(d).

19 *Application of the Diamond State Tel. Co.*, 107 A.2d 786, 793 (Del.1954).

20 203 A.2d 817 (Del.Super.Ct.1964).

21 *Id.* at 832-33.

22 Appellant's Br. at 8.

23 *Id.* at 832.

24 26 *Del. C.* § 512.

25 Tr. at 304-05.

26 Tr. at 230-31, 293-94, 308-09.

27 For instance, Delmarva has agreed to donate $750,000 for job training and business development, to donate $200,000 for the promotion of renewable resources in Delaware, to maintain its current levels of charitable donations for the next six years, and to maintain its operational headquarters in Delaware for the next five years.

28 The powers and duties of the Division of the Public Advocate are set forth in 29 *Del. C.* § 8808. Subsection (d) of that section provides in part:

> The Public Advocate shall have the following powers and duties:
>
> (1) To appear before the Public Service Commission on behalf of the interest of consumers in any matter or proceeding over which the Commission has jurisdiction and in which the Public Advocate deems the interest of consumers requires such participation.
>
> (2) To advocate the lowest reasonable rates for consumers consistent with the maintenance of adequate utility service and consistent with an equitable distribution of rates among all classes of consumers.

29 26 *Del. C.* § 1006(a)(1) a.

30 26 *Del. C.* § 1006(a)(2).

31 Tr. at 186-87.

32 Tr. at 275-80.
33 Tr. at 311-12.
34 26 *Del. C.* § 1006(a).
35 At oral argument, Constellation appeared to change its line of argument away from the "discrimination" tack to another, new argument. It appeared to challenge the market priced supply service provision because it does not include a "margin" as directed by statute. However, this Court declines to address the Constellation's new contention. The briefing deadline for this case was extended no less than four times, from the original date of September 25, 2002, to November 15, 2002. Constellation's new argument was simply submitted too late. The Court also finds that it otherwise lacks merit.
36 Tr. at 293-95.
37 Tr. at 239-42.
38 26 *Del. C.* 1010(a)(2).
39 *Id.*
40 26 *Del. C.* § 1010(a)(2).
41 *Id.*
42 Tr. at 330.
43 *Pre-filed Direct Testimony of Andrea C. Crane* at 18.
44 Appellant's Br. at 20.
45 Appellant's Br. at 19.
46 Commission Order No. 5941 at 31.
47 Tr. at 237.
48 Tr. at 234-36, 245-47.
49 Tr. at 275-80, 311-12.
50 Delmarva analogizes such an undertaking to building a twenty lane highway around Dover to alleviate traffic congestion during Nascar races at Dover Downs. Delmarva's Answer at 19.
51 Tr. at 286, 296-97, 309, 317, 334-38, 345-46.
52 Tr. at 335.
53 26 *Del. C.* 102A.
54 *Id.*
55 *See also In re Delaware Power & Light Co.*, 99 A.2d 270, 274 (Del.Super.Ct.1953).

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TAB 3

2000 WL 36573868 (Del.P.S.C.)
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IN THE MATTER OF THE REVIEW OF A RESTRUCTURING PLAN FOR RETAIL COMPETITION BY DELAWARE ELECTRIC COOPERATIVE, INC., THE DETERMINATION OF RATES TO BE IN EFFECT DURING THE TRANSITION PERIOD, AND COSTS PURSUANT TO 26 DEL. C. §§ 1005(b) AND 1006(b)(1) AND 1007 (FILED SEPTEMBER 15, 1999)

PSC Docket No. 99-457
Order No. 5424

Delaware Public Service Commission

April 25, 2000

APPEARANCES:

On behalf of the Applicant, Delaware Electric Cooperative, Inc.: JANET E. ARNOLD, ESQUIRE, and JOHN TERENCE JAYWORK, ESQUIRE, Hudson, Jones, Jaywork & Fisher

On behalf of the Intervenors: The Division of the Public Advocate: PATRICIA A. STOWELL, The Public Advocate, Delmarva Power & Light Company: RANDALL V. GRIFFIN, ESQUIRE, Conectiv, Old Dominion Electric Cooperative JOHN M. FITZPATRICK, ESQUIRE, RICHARD W. GREGORY, ESQUIRE, and MICHAEL HERN, ESQUIRE, LeClair Ryan and JOHN J. SCHREPPLER, ESQUIRE, West Penn Power Company, d/b/a Allegheny Energy, WILLIAM A. DENMAN, ESQUIRE, Schmittinger & Rodriguez

On behalf of the Public Service Commission Staff: JAMES McC. GEDDES, ESQUIRE, Ashby & Geddes, Rate Counsel

BEFORE COMMISSIONERS: JOSHUA M. TWILLEY, Vice Chairman; JOHN R. McCLELLAND, Commissioner; ARNETTA McRAE, Commissioner
OPINION AND ORDER NO. 5424

BY ORDER OF THE COMMISSION:Joshua M. Twilley, Vice ChairmanArnetta McRae, CommissionerJohn R. McClelland, Commissioner

I. NATURE OF THE PROCEEDINGS

*1 1. On March 31, 1999, the Governor of Delaware signed into law the "Electric Utility Restructuring Act of 1999" (72 *Del. Laws* Ch. 10) (the "Act"). The purpose of the Act is to "expeditiously transform the generation, supply, and retail sale of electricity from an integrated, regulated regime to a competitive enterprise where retail customers will have the opportunity to choose a supplier of electricity." (PSC Order No. 5228 at ¶ 1.) The Act directs the Public Service Commission ("Commission") to set the course for the transition to a retail electric supply services competitive market. Specifically, Delaware Electric Cooperative, Inc. ("DEC"), is required by § 1005(b)(1) of the Act to file with the Commission a restructuring plan for implementing retail competition in its service area.

2. DEC filed its required restructuring plan on September 15, 1999, along with the direct written testimony of seven witnesses: (1) Glen E. Merritt, Vice President of Financing and Administration; (2) Joseph Bartolone, Jr., President of Utility Services Corporation; (3) Daniel M. Walker, Old Dominion Electric Cooperative's Vice President of Accounting and Finance; (4) John W. Rainey, Director of Rates and Regulation for Old Dominion Electric Cooperative (hereinafter "ODEC"); (5) James H. Drzemiecki, Director of the Strategic Change of Utilities with Price Waterhouse Coopers, LLP; (6) Jack Gaines, Vice President and Manager, Utility Rate and Finance Services Department for Southern Engineering Company; and (7) J. William Andrew, Vice President, Engineering and Operations Division, DEC.

3. By Order No. 5228, the Commission initiated this docket on September 28, 1999, to begin review of the required plan and open the corresponding rate proceeding (§ 1006(b)). The Commission appointed Hearing Examiner G. Arthur Padmore to conduct evidentiary hearings and report his proposed findings and recommendations.

4. Pursuant to the Commission's Order, the Commission's Secretary published notice of DEC's filing. [1] The following parties were granted leave to intervene in the proceedings: Delmarva Power & Light Company ("Delmarva"); Old Dominion Electric Cooperative ("ODEC"); and West Penn Power Company, d/b/a Allegheny Energy ("AE"). The Division of the Public Advocate ("DPA") exercised its statutory right to intervene pursuant to 29 *Del. C.* § 8808(g).

*2 5. On November 17, 1999, Staff filed the testimony of seven witnesses addressing issues raised by DEC's proposed restructuring plan: (1) Rajnish Barua, Ph.D., the Commission's Regulatory Policy Administrator; (2) Brian Kalcic, the principal of Excel Consulting; (3) Richard A. Rosen, Executive Vice-President of the Tellus Institute, Director of the Energy Group, and Manager of its Electricity Program; (4) Richard A. Latourette, a Commission Public Utilities Analyst; (5) Kevin S. Neilson, a Commission Public Utilities Analyst; (6) D. Kevin Sigafoos, the Commission's Regulatory Economist; and (7) Jennifer J. S. Tietbohl, a Commission Public Utility Analyst.

6. The DPA submitted the written testimony of two witnesses: (1) Andrea C. Crane, a principal with The Columbia Group; and (2) Christopher R. Cook, principal of E3 Energy Services LLP.

7. ODEC submitted the written testimony of two witnesses: (1) Jackson E. Reasor, Jr., President, Chief Executive Officer of ODEC; and (2) Joseph B. Wharton, a principal of the Brattle Group.

8. On December 8, 1999, DEC submitted the rebuttal testimony of the previous seven witnesses, as well as that of two additional witnesses: (1) Michael Barrett, a principal of Ernst & Young; and (2) Carl F. Lyon, Esquire, an attorney with Orrick, Herrington & Sutcliffe. Staff submitted the rebuttal testimony of Dr. Richard A. Rosen.

9. On December 13 and 14, 1999, with duly publicized notice, the Hearing Examiner conducted an evidentiary hearing on the DEC restructuring plan. The parties presented both written and oral witness testimony (subject to cross-examination). No DEC customer/member attended the hearings nor submitted any comment to the DEC proposals. At the conclusion of the hearings, the record consisted of 38 exhibits and a 623-page verbatim transcript of the proceedings. The parties then filed initial and reply briefs.

10. On January 21, 2000, DEC and Staff submitted a proposed "settlement" of the majority of the process-related issues that the parties elected to resolve through negotiation rather than through the hearing process. (Ex. I to HER.) The Public Advocate is the only party of those appearing which has indicated any objection or opposition to various parts of the proposed settlement. While the Hearing Examiner considered the settlement to be facially reasonable, the agreement was viewed as an "understanding between the signatories" and not in anyway binding on the Commission.

11. On January 27, 2000, the Hearing Examiner issued his proposed Findings and Recommendations.

12. On February 10, 2000, DPA, DEC, and ODEC filed exceptions to the Hearing Examiner's Findings and Recommendations; Staff and DP&L filed letters seeking clarification of certain issues addressed in the Hearing Examiner's Report.

13. On February 22, 2000, the Commission met to consider the record, the Hearing Examiner's Proposed Findings and Recommendations and the parties' exceptions thereto, and to deliberate in open session regarding DEC's proposed restructuring plan. Chairman McMahon and Commissioner Puglisi recused themselves from the deliberations and decisions made on February 22, 2000.

*3 14. On February 28, 2000, the Commission issued an Order setting forth the resolution of the issues before it concerning DEC's proposed restructuring plan, noting that the Order would be supplemented at a later time. This is the Commission's Opinion and Order supplementing its February 28, 2000, Order.

II. STATEMENT OF FACTS

A. Background:

15. On March 30, 1999, the Governor of Delaware signed the Restructuring Act into law. The purpose of the Act is to provide for transition to retail electric supply via the competitive market. The Act requires DEC to provide a plan for such a transition. To be included in that plan are proposed tariffs and schedules that provide for:
(a) separate prices or rates for electric supply, transmission, distribution and other services (which may be combined for billing purposes);

(b) proposed procedures for allowing retail customers direct access to electric suppliers;

(c) revised tariffs and rate schedules;

(d) a proposed Competitive Transition Charge ("CTC") which reflects a proposed method, recovery plan, and calculation of DEC's Stranded and Transition Costs (as are defined by 26 *Del. C.* § 1007); and

(e) standards to measure and ensure reliability after retail competition is implemented.

16. Furthermore, pursuant to § 1006(b)(1) of the Act, the Commission is directed to make rate determinations which:
(a) establish the "retail market price" for electric supply service for each customer rate class;

(b) recalculate base and fuel rates based on a March 31, 2000 benchmark;

(c) establish a Competitive Transition Charge that will permit DEC to recover allowed Stranded Costs and Transition Costs over the transition period;

(d) approve the separation of the above rates into rates for electric supply, transmission, ancillary, distribution, nuclear decommissioning costs, Competitive Transition Charge, and other services; and

(e) calculate an additional surcharge or credit for accrued, but previously deferred, fuel costs.

17. Some issues requiring resolution, but which were not included in the Act, were addressed in a "Side Letter" negotiated by members of AFFECT[2] and representatives of the Governor's office. The record in the Delmarva restructuring proceeding indicated that neither the Commission nor its Hearing Examiner was bound by terms and conditions contained in the Side Letter. At the conclusion of the Delmarva proceeding, the Commission recognized the Side Letter "as a partial settlement permitted under 26 *Del.C.* §512, the economic terms of which [were] incorporated into [the Delmarva] decision." (Opinion and Order No. 5231 at 26, dated September 28, 1999, PSC Docket No. 99-163).

*4 18. The Side Letter contains the following provisions applicable to DEC:
(a) DEC shall be permitted to recover all reasonably incurred, non-mitigable Stranded and Transition Costs, as defined in the Act ("S&T Costs"). The amount and method of determining DEC's S&T Costs shall be decided by the Commission.

In determining DEC's S&T Costs, the Commission should give due consideration to the costs incurred by DEC under its power purchase contract with ODEC.

(b) Beginning April 1, 2000, there shall be no change in DEC's electric rates for a 5-year period ending March 30, 2005, except for (i) the deferred fuel clause true-up credit or charge described in the Act; and (ii) any Commission-approved adjustments for extraordinary costs, as provided in the Act.

(c) When setting rates for regulated services at the end of the transition period, pursuant to § 1007(b)(2)(iv) of the Act, the Commission should consider: (i) changes in federal, state, or local tax rates; (ii) changes in law and regulations (including environmental regulations) affecting DEC's S&T Costs; and (iii) changes in nuclear decommissioning costs not known to DEC at the time its S&T Costs were first determined by the Commission.

(d) The parties to the Agreement share the objective of avoiding (i) the shifting into Delaware of S&T Costs attributable to members of other cooperatives affiliated with ODEC; and (ii) the shifting outside of Delaware of S&T Costs attributable to members of DEC. Accordingly, except in unusual circumstances where it would be appropriate to do so (such as the adoption of legislation in another jurisdiction which has material impact on DEC members with respect to the treatment of S&T Costs), the Commission should endeavor to ensure that there will be no shifting of S&T Costs among jurisdictions.

19. As a cooperative, DEC is required to provide electric service to all its members at cost, meaning that it only retains the amount of revenues necessary to cover operating expenses such as purchasing power, operating the distribution system, and servicing debt obligations. (HER at 9.) DEC is a not for profit entity with no separate body of independent shareholders. Thus, once DEC pays its requisite expenses and taxes, what revenues (whether termed as profits or margins) remain are held as "patronage" in special "capital accounts" representing each customer/member's ownership interest in DEC, and when DEC is financially able, redistributed to DEC's customer/members. *Id.*

20. DEC is also subject to the mortgages and loan contract with the United States Department of Agriculture's Rural Utility Service ("RUS"), whereby DEC must set its rates so that it collects sufficient revenues (Times Interest Earned Ratio, hereinafter "TIER") to meet interest payments plus a margin. (HER at 10.) The TIER requirement provides the necessary assurance to bond holders and other lenders to lend money to DEC at costs lower than in the equity markets and is the nucleus of DEC's mortgage and loan contracts with RUS and the National Rural Utilities Cooperative Finance Corporation ("CFC"). *Id.* Typically DEC is required to maintain a minimum TIER of 1.5. *Id.*

*5 21. DEC is solely a distribution cooperative. It receives all its generation and transmission from ODEC (also a not for profit cooperative), in which DEC holds a 1/12 th ownership interest. DEC signed a 45-year "all-requirements contract" with ODEC in 1983, granting ODEC the exclusive right to supply DEC's power, requiring DEC to pay for all power supplied, if any. (HER at 10.) This contract was later amended and restated as the "Wholesale Power Contract" ("WPC") by ODEC and its members.

B. The DEC Proposed Restructuring Plan:

1. Proposed Tariff

22. The Act requires DEC's proposed restructuring plan to provide a proposed revised electric service tariff. Staff and DEC met to discuss various concerns Staff had regarding some of DEC's proposed tariff changes. Staff was concerned that the proposed change to § 9.7 (Cooperative Liability and Other Proposed Language Changes) appeared to be inconsistent with provisions of the Restructuring Act. After considerable discussion with Staff, DEC has agreed to adopt in its proposal the original tariff language of § 9.7 of the tariff filed on November 16, 1992 (Ex. 35) Further, DEC and

Staff met in order to address various language and definitional changes necessary to keep the tariff consistent with the Act and ensure a smooth transition for DEC's customer/members. In addition, DEC proposed to close certain time of use service classifications; specifically, R-TOU-ND and GS-TOU-DR. Although no party objected to this proposal, and the Hearing Examiner adopted it, the Commission has decided to defer the issue for the reasons stated herein. (*See discussion infra* III B, pgs. 30-31).

2. Code of Conduct

23. DEC included a Code of Conduct ("Code") in its proposed restructuring plan. (Ex. 6, Sch. 2.) The parties DEC, DPA, and Staff suggest that the Code be examined in a separate proceeding. In particular, DEC favored a proceeding for review of its Code separate from any proceeding regarding Delmarva's Code. In addition, DPA suggested that DEC and ODEC be considered "affiliates," a term which DPA contends that the Commission is authorized to define differently for a distribution entity than for a supply entity. DEC contended that ODEC is not an affiliate since it fails to meet the 10% ownership requirement of PSC Regulation Docket No. 49.[3] Additionally, DEC suggested that the Code proceeding result in a final Commission Order prior to DEC's phase three implementation on April 1, 2001.

3. Cost Accounting Manual

24. Along with the Code, DEC submitted a Cost Accounting Manual ("CAM") designed to ensure that DEC's management of its accounts complies with its Code. All the parties agreed that the CAM should be addressed in a separate proceeding later in the year, but completed prior to April 1, 2001.

4. Supplier Agreement

*6 25. As required by § 1005(b) of the Act, DEC submitted, within its proposed restructuring plan, an Electric Supplier Agreement ("ESA"). DEC's supplier agreement includes general "standards for creditworthiness" for electric suppliers.

26. DPA witness Crane took issue with the creditworthiness provision, asserting that only the Commission is responsible for applying financial restrictions upon electric suppliers. Staff also took issue with DEC's supplier agreement. First, Staff noted inconsistencies between definitions in the supplier agreement and the proposed tariff. Second, Staff asserted that DEC needs to have a process in place for performing balancing and settlement at the inception of competition. DEC responded that it developed a draft manual for such a process to be in place at the inception of competition and reiterated its commitment to insuring all electric suppliers are treated fairly. Both Staff and DEC agree that the supplier agreement is an issue that should be decided mainly between DEC and the suppliers themselves, and that the Commission only need acknowledge the proposed agreement. The Hearing Examiner reiterated that the proposed agreement was an "understanding among the signatories, ... [not binding] the Commission in any way and which does not require the Commission to surrender any of its authority or to prejudge any of the issues that are resolved or left open." (HER at 18.)

5. Integrated Resource Plan

27. By Order No. 3756 (PSC Regulation Docket No. 35), the Commission adopted guidelines for DEC to use in developing the Integrated Resource Plan ("IRP") requiring DEC to file an IRP with the Commission every two years. DEC and Staff share the belief that such IRPs have become obsolete with the inception of retail choice in Delaware and suggested that such requirements be eliminated.

6. Process Issues

28. A host of business processes stand to be affected and will need to be adapted to the environment of competitive electric supply and generation in Delaware. For incumbent utilities, the Act requires procedures to effectuate direct access for all electric suppliers. The procedural areas in need of adaptation prior to implementation of customer choice include: customer education, phase-in and enrollment, supplier switching, supplier withdrawal, load balancing, settlement and load profiling, and electric supplier interactions.

29. DEC proposed that all the process issues be addressed by all interested parties in the context of the Delaware Process Review Committee ("DPRC"), composed of representatives from the Staff, DEC, DPA, and other interested parties. DEC further suggested that the DPRC be responsible for finalization of the process issues necessary for implementing retail choice. Staff concurred. For unresolvable issues, DEC suggested separate, expedited consideration to ensure that DEC can implement final business rules and processes consistent with the phase-in schedule of the Act.

*7 30. **Customer Education** - DEC proposed using materials already developed by the Delaware Customer Education Work Group ("CEWG") as a foundation for its educational program. DEC also claimed that the Act fails to provide adequate funding for such programs, and, thus, it plans to use its customer/member newsletters for education. (DEC at 30.) Relying on examples from various DEC newsletters, Staff suggested that DEC's presentation of the opportunities available to customers regarding retail choice may not have been presented objectively and that more effort should be made by DEC to present a more balanced view.

31. **Phase-In and Notification** - The Act provides a schedule for DEC's phase-in for customer choice. Customers with a 1000 kW or more monthly peak load are eligible to choose an alternative electric supplier on April 1, 2000. Customers with a 300 kW or more monthly peak load are eligible to choose an alternative electric supplier on July 1, 2000. All customers are eligible to participate on April 1, 2001. DEC proposes to notify customers of eligibility through mailings sent to customers, as they become eligible, containing instructions on how to request an enrollment package if interested in participating in retail choice. Neither the parties nor the Hearing Examiner had any objection to DEC's proposal.

32. **Enrollment** - DEC proposed requiring its customer/members to pay a charge of $4.75, for each enrollment package for the stated reason that DEC believes that cost of generating this material ought to be borne by the customer/members who request it, as opposed to those who do not. Both Staff and the DPA strongly opposed DEC's position regarding the need for customers to pay for enrollment packages. The DPA argued that this type of charge created a disincentive for customers to want to shop for electric energy and further stated that given the nature of the data, customers should have the right to periodically obtain such information free of charge. As a compromise, the DPA suggested that DEC be required to provide, once annually, each customer with historic usage data (including interval data), free of charge. The DPA did not oppose a charge to customers who made additional requests. Staff also viewed DEC's proposed charge for enrollment packages as a direct barrier to customer choice. Staff also maintained that such information should be available to customers free of charge (as enrollment packages are in the Delmarva case - PSC Docket No. 99-163).

33. DEC responded by offering a 2-level proposal providing: (a) that DEC will bear the costs of enrollment packages through the inclusion of those costs in the Transition Costs coupled with mitigation through operational savings; and (b) DEC will provide customer/members with an additional billing period within which to make a supplier choice prior to the "Customer Retention Period" going into effect. [4]

*8 34. **Supplier Switching** - The majority of matters involved in this issue, changing to a different electric supplier after an initial supplier is selected, were addressed and resolved within the DPRC.

35. **Supplier Withdrawal** - This issue was also addressed by the DPRC. However, DEC proposed that if an electric supplier elects to terminate service to an entire rate class of customer/members, the supplier is required to provide a minimum of 60 days' notice to the affected rate class, the Commission, and the DPA. The parties accepted DEC's proposal in the context of the DPRC.

36. **Metering and Billing** - To ensure that customer/members are billed appropriately under retail competition, and to ensure that payments are accurately posted, DEC proposed a 6-step customer billing process, where a customer/member has selected an Electric Supplier:
(1) Electric Supplier provides rate structure and rules to DEC;

(2) DEC sends a consolidated bill to customer/member;

(3) DEC notifies electric supplier that bill was sent and provides meter data;

(4) customer/member pays DEC;

(5) DEC provides payment information to electric supplier; and

(6) DEC provides payment share to electric supplier.

DEC maintained that the process is consistent with the collection procedure adopted in the Delmarva restructuring. None of the other parties opposed DEC's billing plan.

37. **Physical Connection/Disconnection of Service** - DEC proposed that it be the sole entity responsible for physical connection/disconnection of customer service, since it will continue to own and maintain the distribution system and metering equipment. DEC maintains that it will only disconnect service in instances of non-payment of DEC charges, but not for nonpayment of electric supplier charges (that is between the customer/member and the chosen supplier). None of the other parties opposed this proposal.

38. **Load Profiling** - New electric suppliers entering the marketplace in the wake of retail competition will need DEC customer information for energy estimation, scheduling purposes, and transmission requirements. To meet this need, DEC stated that it is installing interval meters on the premises of all customer/members with monthly peak demands at or above 300 kW, to record actual historic load information to be provided to suppliers. DEC proposed using load profile studies for customers having a peak monthly demand below 300 kW, which will serve as a proxy for actual load information and will be developed by DEC and ODEC. The proposed load profiles are not yet developed and will not be necessary until phase three implementation (April 1, 2001). Further, DEC requested that it be permitted to submit its load profiles this year. None of the other parties opposed DEC's proposal.

39. **Balancing and Settlement** - As of the date of deliberations, DEC had not developed its own balancing and settlement process. DEC stated that it anticipates that it will be more cost effective for ODEC to perform that function since it receives all of the billing information from PJM and Delmarva. In addition, DEC points out that having ODEC perform balancing and settlement services mitigates the need for additional expenditures that would be required if DEC were to perform those same services for its members. Although Staff agrees that reliance on ODEC should result in more accurate estimations, the actual methodology and/or implementation process for balancing and settlement has not been reviewed by other parties to the proceeding and Staff is concerned that a timetable for the completion of implementation of a balancing and settlement process needs to be established.

*9 40. **Dispute Resolution** - DEC proposed that any disputes arising between customer/members and electric suppliers be resolved between themselves. Although Staff did not take a position directly on this issue, it did suggest that the remaining issues would be reviewed by DPRC and, to the extent they are not resolved, they should be brought directly to the Commission. (Staff at 14.)

41. **Supplier Interaction Protocols and Electronic Data Exchange** - This issue was deferred to the DPRC and has yet to be addressed. DEC proposed that the DPRC continue to address the issue and in the event of an impasse, to address the issue in an expedited proceeding so that final business rules and processes consistent with the Act, may be implemented by DEC.

7. Customer Retention and "Gaming"

42. This issue proved to be a bone of contention between DEC and Staff and the DPA. In § 1010(c), the Act directs the Commission to promulgate rules and regulations governing the minimum amount of time a customer must accept service from its incumbent utility. It also directs the Commission to set the amount to be assessed against a customer electing to shop for competitive supply service, who then later returns to the incumbent utility.

43. DEC proposed a 12-month retention period to protect customers who do not switch, from the financial impact resulting from those who switch suppliers and then return to the incumbent utility. Staff opposed DEC's proposal on the basis that a 12-month retention period constitutes a significant barrier to competition and choice. Further, Staff contended that DEC failed to show clear evidence of "customer gaming" being a problem in other jurisdictions. Staff suggested that the Delmarva retention periods be applied to DEC. The DPA shared Staff's opposition to the retention period for similar reasons.

44. DEC cited "profound differences" between its customer base and that of Delmarva. Specifically, DEC claimed it has a significantly lower percentage of its customer base, than does Delmarva, with demand peaks of 300 kW or greater. In an effort to address Staff concerns, DEC proposed an alternative which provides customer/members with an additional billing period within which to select another electric supplier before being subject to the 12-month retention period and being forced to stay with DEC.

45. Staff maintained its contention of DEC's failure to offer evidence of customer gaming, asserting DEC's interests must be weighed against the customers' right to choose. Staff maintained that any such retention period should be used only as a last resort. Moreover, Staff witness Tietbohl noted that DEC's alternative proposal served to worsen the situation rather than improve it. According to Staff witness Tietbohl, the additional billing period of 30 days would only provide for more opportunity facilitating the summer gaming issue.

46. The DPA asserted that DEC was asking the Commission to solve a problem not yet in existence. DPA witness Crane indicated that such an issue had not been a problem in other jurisdictions, thus DPA concluded, like Staff, that the Commission should apply the same retention period that it used in the Delmarva case for residential customers. [5]

8. Rate Unbundling

*10 47. The Act requires DEC to set unbundled rates for its customer/members during the transition period, pursuant to the principles established under § 1006(b)(1). The Act further requires that retail rate levels effective during the transition period be set by the Commission without conducting a rate base case.

48. This issue proved to be contentious as both DEC and Staff vigorously disputed each other's interpretation of the Act's unbundling requirements. Staff interpreted the Act to require the retail market price, CTC, and distribution component of DEC's rates to be set as constants, remaining so throughout the transition period. DEC, however, interpreted the Act to require it to estimate retail market prices for each year of the transition period, and not to set its retail market prices at a constant value. In addition, DEC maintained that since its projected stranded costs will decrease each year of the transition period, reaching zero in the final year of the transition, that its CTC charges should decrease and its distribution charges should correspondingly increase during the transition period.

49. Staff maintained that DEC failed to file a set of tariffs that could be used by the Commission to unbundle DEC's rates, and that the rates proposed by DEC contained input errors and failed to reflect adjustments that DEC's own witness agreed should be made. Staff maintained that the methodology it proposed is the same as the methodology approved by the Commission in the Delmarva deregulation case. Additionally, Staff stated that DEC's distribution rates could not be permitted to fluctuate through the transition period since that would alter the fundamental nature and intent of unbundling, which is to identify the portion of DEC's current rates subject to competition. Staff further maintained that because distribution charges cannot fund stranded cost recovery, those rates should not rise through the transition period as the CTC charges decline. Lastly, Staff reiterated that in the Delmarva restructuring, the Commission fixed a single set of distribution rates for the transition period for each Delmarva rate class.

9. Retail Market Price ("Shopping Credit")

50. This issue presented yet another area of fundamental divergence and opposition between the parties. The crux of disagreement concerned the appropriate methodology for determining the shopping credit, as well as the level of shopping credits. DEC and ODEC supported DEC's proposed residential shopping credit of $0.03381 per kWh for the first year of the transition period. DEC maintained that the shopping credit should be set in accordance with its proposed methodology. DEC also maintained that the shopping credit could not be a residual value, but rather an established value based on the actual cost of electric supply. Further, DEC suggested that the Staff/DPA proposed shopping credits would be set at inflated levels which would encourage customer/members to leave DEC due to "a false price signal." (Ex. 14; DEC RB at 23.)

***11** 51. ODEC suggested that the Commission's main decision was to determine the shopping credit and that if the Commission followed the method laid out in Order No. 5231, DEC's revenue would be sufficient regardless of the CTC used. Moreover, ODEC argued that the FERC "filed rate doctrine" mandates that ODEC continue to charge DEC the rates determined according to that FERC formula. ODEC further argued that since DEC's rates are lower than Delmarva's, DEC's shopping credit should be lower than that set for Delmarva. (ODEC at 18.) Finally, ODEC maintained that because DEC is a not-for-profit cooperative, its retail margin should be calculated as zero.

52. The DPA advocated that the primary concern of any utility restructuring plan is the determination of the shopping credit, since without that, customers have no incentive or ability to shop. The DPA asserted that the shopping credit should include both the wholesale electric market price and a reasonable allowance for retail margin. The DPA recommended that the shopping credit be based on the embedded generation costs of the utility, less any stranded costs, plus reasonable retail adder. The DPA asserted that DEC incurs administrative, general, marketing, and other ancillary costs and quantified retail costs at $0.00226 per kWh (advocating that this figure be considered in the establishment of any shopping credit). (DPA RB at 8-9.)

53. Staff reviewed DEC's proposed unbundling methodology and concluded that certain changes be incorporated within it to derive an appropriate set of unbundled rates. (Ex. 28 at 2.) Under Staff's proposed methodology, class shopping credits are determined as the residual Purchase Power Costs ("PPC") revenue after the removal of all transmission related services, including ancillary and nuclear decommissioning components. This approach increases shopping credits for all classes to levels on par with those offered by Delmarva and other PJM utilities. (*See* Sch. Bk-5; *see also* Ex. 28 at 11; Staff at 12-13.)

10. Reliability

54. DEC claimed it complied with § 1005(b)(1) of the Act (requiring DEC to include standards for reliability to measure variations in service reliability after retail competition) by outlining the reliability reporting it performed in the past. DEC also proposed future measures to gauge system reliability. (HER at 52.) DEC proposed three future methods:
(1) use of Electric Power Research Institute standard reporting indices;

(2) continue to report reliability measures to the Commission; and

(3) continue monthly reviews of reliability indicators to assure continued performance at or above historic levels. (*Id.*)

Staff found DEC's reliability standards to be reasonable and appropriate, as did the Hearing Examiner.

11. Transition and Stranded Costs

55. The Act, under § 1007(d), allows DEC to recover its reasonably incurred, non-mitigable stranded and transmission costs. In moving to a new, competitive market, it is anticipated that DEC will incur certain costs associated with implementation of the Restructuring Act. These "transition costs" include the cost of software and equipment to allow for a competitive retail market, as well as personnel costs, costs of purchasing, and other modifications of physical plants that may be required to make the transition to a competitive electric supply market.

*12 56. DEC estimated it's one-time transition costs at $830,000. (Ex. 6 at 11 and Sch. GEM-1; DEC at 62-63.) DEC plans to mitigate some of these costs with operational savings from its own operations, as well as from ODEC's. DEC proposes that the remaining balance of these transitional costs be deferred and collected in the next base rate proceeding. Staff did not oppose DEC's proposal, but cautioned that the deferral should not be viewed as a presumption that such costs should be recovered in DEC's next base rate case. (Staff at 14.) The DPA, however, opposed DEC's proposal, arguing that ODEC would pass a 4% annual reduction in demand costs to DEC, but the same reduction would not be passed to DEC customer/members since rates under the restructuring legislation are frozen for the transition period. According to DPA, this cost reduction will create additional sources of revenues which can be used to offset DEC's transition costs. In addition, DPA argues that some of the transition costs (specifically, $285,000 per year) reflect ongoing operational costs and should not be collected in this manner. Accordingly, DPA suggests that DEC's request for deferred ratemaking and accounting treatment for these transition costs be denied. (DPA at 20.)

57. **Stranded Costs** - This was clearly the most contentious issue between the parties. Despite the parties' shared agreement that the Side Letter and Act allow DEC to recover stranded costs, the parties fundamentally disagreed on the proper quantification and calculation of DEC's stranded costs. The core dispute centered on DEC's claim of $81.03 million of stranded costs (supported by ODEC), and Staff's conclusion -- shared by DPA -- that DEC has no positive stranded costs.

58. There is general agreement among the parties that stranded costs are those generation costs that the utility would have recovered under a traditional regulatory framework, which are no longer capable of recovery in a competitive market place. Stranded costs, therefore, are that portion of the embedded generation costs that exceed the market price for those assets and are, therefore, uneconomic in a deregulated environment.

59. The parties generally agreed that the Lost Revenues Approach ("LRA") was an appropriate starting point for calculation and quantification of stranded costs. DEC and ODEC, however, advocated an adjustment of the LRA due to DEC's not-for-profit cooperative make-up. DEC proposed a "Cash to Market" Approach ("CMA"), based on an amount required to bring rates to market prices in 2004. (DEC at 71.) The CMA identifies the amount of additional funds necessary for ODEC to collect before implementation of retail competition in Virginia to reduce prices to market levels.

60. DEC asserted that ODEC's Strategic Plan Initiative automatically recovers ODEC's alleged stranded costs, which are included in the wholesale rate, and that the amount of stranded costs "floats," or automatically changes as the wholesale rate changes in relation to market power costs. Thus, DEC contended that quantification of stranded costs is unnecessary since the wholesale rate self-corrects over time.

*13 61. The DPA testified that the CMA approach was too static because it only examines costs at only a single point in time -- 2004 -- thereby ignoring occurrences after that date. Staff also disagreed with using the CMA, citing that CMA's fundamental flaw is its failure to examine costs over the entire useful life of the facilities being evaluated. Both Staff and DPA advocated use of the LRA, an approach which examines the difference in cash flows when comparing the future market value of a utility's electric generation in a deregulated environment with the net book value of that same generation in a regulated universe.

62. Further, both Staff and the DPA asserted that the DEC/ODEC calculation of stranded costs was wrong, claiming that it did not comport with the Act. (Staff RB at 10-11.) Staff contended that recovery for these costs for a cooperative should be the same as for an investor-owned-utility (IOU). DEC and ODEC attempted to rebut Staff's point by asserting that DEC's by-laws require it to always sell at cost and, therefore, DEC could not take advantage of higher-market prices by selling at prices above its actual cost.

63. A collateral issue in determining the appropriate level of stranded costs for DEC involves which market prices should be used in the calculation. DEC and ODEC advocated the use of VACAR prices because ODEC charges DEC for power using a postage stamp rate encompassing costs from all of ODEC's power sources. They claimed that failure to use the VACAR prices would result in improper cost shifting out of Delaware. (DEC RB at 27-28.) Staff and the DPA advocated the use of PJM [6] market prices for calculating DEC's stranded costs, due to DEC's physical location within Delaware. Staff and the DPA further argued that to use the VACAR prices would result in an improper cost shifting into Delaware.

64. In an attempt to mitigate projected stranded costs, ODEC designed and adopted the Strategic Plan Initiative ("SPI") to decrease ODEC's embedded generation costs to market levels by 2004 (the beginning of competition in Virginia). Under SPI, revenues collected are applied to accelerate payment of ODEC's debt, thereby decreasing its interest costs and driving ODEC's overall cost structure towards market levels by 2004. Like DEC, ODEC is a cooperative and any over-collection is returned to the customer/members.

65. Staff had three main objections to the SPI: (a) it violates § 4(b)(i) of the WPC; (b) it violates FERC requirements; and (c) the Commission was not informed of, nor did it approve, recovery of revenues collected under the SPI from DEC customer/members. The DPA asserted that no further SPI amounts should be collected from DEC customer/members, and that ODEC began collecting stranded costs through SPI more than two years ago, prior to any finding that any stranded costs actually existed.

*14 66. In response, DEC suggested that FERC relies on the ODEC Board to oversee the implementation of rates charged under the FERC formula and, thus, the SPI did not violate FERC rules/ratemaking procedures. Moreover, DEC asserted that this Commission was adequately informed of the SPI during a meeting with several Staff members on October 19, 1998. Further, DEC stated that SPI allows ODEC to legitimately "mitigate" generation related costs.

67. In addition, DEC and ODEC claimed that under the "filed rate doctrine" the Commission's review of the SPI rates is prohibited. ODEC suggested that since the rate formula (under which the SPI was included) was previously accepted by FERC as the "lawful filed rate," it allows ODEC to set rates that collect SPI charges from its member cooperatives. Thus the inclusion of the SPI component as part of the rates derived under the FERC formula is valid and should not be viewed as an additional charge. (Ex. 12 at 5-14; Ex. 11 at 12-13.) ODEC further argued that because DEC purchases all its power from ODEC, those costs are already unbundled from DEC's existing rates. In its exceptions to the Hearing Examiner's Report, Delmarva supported the ODEC/DEC view of the filed rate doctrine.

C. The Hearing Examiner's Proposed Findings and Conclusions.

68. The Hearing Examiner recommended:

• that the Commission adopt DEC's proposed revised electric service tariff and, with respect to the proposed language and definitional tariff changes, the Commission direct DEC to meet with Staff (and any other interested party) to modify the proposed tariff to make it acceptably clear and consistent with the Act. Additionally, it is also recommended that the Commission require DEC and Staff to report the results of their meeting to the Commission within 15 days of the Commission's final Order in the proceeding;

• that the Commission adopt the settlement between DEC and the DPA regarding net metering set forth in Ex. 3 at Sch. JWA-9 (HER at 83);

• that the Commission initiate a separate docket to consider a separate Code of Conduct for DEC (concluding with sufficient time for the Commission to issue a final Order prior to April 1, 2001); and that until the Commission gives final approval to DEC on its Code of Conduct, it should require ODEC and DEC to maintain separate and complete documentation of any and all joint sales, marketing arrangements, as well as exchanges of DEC customer information (HER at 83);

• that the Commission require a review of the Cost Accounting Manual for DEC to be performed at the same time the Code of Conduct is reviewed (HER at 83);

• that the Commission adopt DEC's proposed Electric Supplier Agreement and manual for Electric Suppliers (HER at 83);

• that the Commission terminate the IRP requirements imposed by PSC Docket No. 35, and require DEC to file an annual report similar to that required for Delmarva in accordance with the approved partial settlement agreement in PSC Docket No. 99-163 (HER at 83-84);

*15 • that the Commission adopt the process issues incorporated in the settlement agreement (attached to HER as Ex. I) (HER at 84);

• that the Commission authorize the continued use of the DPRC to address the process issues necessary to implement retail choice but not resolved in this proceeding, and require the parties to report their progress in resolving such issues to the Commission on a monthly basis (beginning one month after issuance of a final Commission decision on the docket) (HER at 84);

• that the Commission permit DEC to proceed with customer education using materials already completed by the CEWG, but prohibit DEC's dissemination of customer education materials not derived from the aforementioned sources among its customer/members until those materials have been reviewed in the Code of Conduct proceeding (HER at 84);

• that the Commission adopt and approve as reasonable DEC's proposed customer notification procedure (HER at 84);

• that the Commission adopt and approve the proposed resolution of the enrollment issues as set forth in the settlement agreement with the addition that customer usage information be provided to customers without charge at least once each year upon a customer's request (HER at 84);

• that the Commission approve the proposed resolution of supplier switching issues as set forth in the settlement agreement (HER at 85);

• that the Commission approve the proposed settlement's resolution of the Supplier Withdrawal issue (HER at 85);

• that the Commission find reasonable and approve DEC's proposed 6-step billing process, bill format, and payment processing proposal (HR at 85);

• that the Commission find reasonable and approve DEC's proposal that it be declared the sole entity with responsibility for physical connection/disconnection of customer service (HER at 85);

• that the Commission approve DEC s proposal that it be allowed to submit its load profiles during the current year, well in advance of the commencement of phase three implementation (HER at 85);

• that the Commission direct DEC to provide (no later than the Commission's final Order in this proceeding) its proposed procedures for the balancing and settlement process to all the other parties However, if such procedures cannot be promptly resolved by the DPRC, Staff, DEC, and the other DPRC members should present their recommendations to the Commission no later than February 15, 2001 in an expedited proceeding (HER at 85);

• that to the extent that the parties are unable to resolve issues relating to dispute resolution and supplier interaction protocols and data exchange within the context of the DPRC, these issues be addressed in an expedited proceeding before the Commission (HER at 86);

• that the Commission order that for returning customers with monthly demand below 300 kW, no retention period applies, and for returning customers with a monthly peak demand of 300 kW and above, a 12-month retention period applies (HER at 86);

*16 • that, except for Staffs proposal to use updated load factors, the Commission adopt Staffs rate unbundling methodology, and that the Commission direct DEC to work with Staff and promptly file unbundled rates for each year of the transition period that are consistent with the findings of this report (HER at 86);

• that thc Commission find reasonable Staffs proposed shopping credits and that DEC use Staffs rate unbundling methodology to calculate its unbundled rates (including DEC's retail market price) (HER at 86);

• that the Commission direct DEC to work with Staff to calculate appropriate unbundled rates for each year of the transition period which should be forthwith filed with the Commission (HER at 86);

• that the Commission approve DEC's proposals concerning reliability standards (HER at 87);

• that the Commission permit DEC to defer its one-time transition costs for accounting purposes, to be considered in DEC's next rate case, but with the specific condition that the deferral not be construed as guidance with respect to whether such costs could or should be recovered in that proceeding (HER at 87); and

• that with respect to DEC s stranded cost claim, the Commission adopt and approve the following findings: (a) that DEC's unbundled rates reflect a zero value for stranded costs; (b) that in calculating DEC's stranded cost determination, PJM prices are appropriate; (c) that the SPI is an unauthorized rate and should be discontinued forthwith and all such unauthorized amounts should be refunded to DEC's customer/members; and (d) that ODEC began collecting stranded costs from DEC over two years ago, prior to any finding by this Commission that stranded costs existed, and that because DEC has no stranded costs, no further SPI rates should be collected from DEC customers (HER at 87).

III. FINDINGS AND OPINION

A. The Commission's Responsibility Under the Act

The Act instructs the Commission to review the restructuring plan submitted by DEC and, after an evidentiary hearing, issue an order by February 28, 2000 adopting the plan as filed or modifying the plan as appropriate. 26 *Del.C.* §1005(b)(2). The Act also directs the Commission to determine the rates that will be in effect during the transition period on an unbundled revenue-neutral basis, without conducting a base rate case. *Id.* §1006(b)(1). Therefore, the rates that are currently in effect (and which were previously approved by the Commission) will be the rates that will be effective during the transition period; the only difference is that those rates will be unbundled into their component parts. (*See* Order 5366, Exh. A).

B. Revisions to Electric Service Tariff

As part of DEC's proposed restructuring plan, certain revisions have been proposed to its electric service tariff, including the elimination of certain time of use rates (R-TOU-ND and GS-TOU-DR). The Hearing Examiner and the parties have agreed to accept the proposed revisions and the Commission will as well, except to the extent that DEC's revisions require modification to either its load management or time of use offerings. As noted, DP&L's restructuring specifically required the creation of an additional time of use tariff. Although DEC was not included in this portion of the restructuring legislation, there appears to be no reason why its time of use offerings need, at this time, to be closed. Accordingly, we defer decision on any tariff modifications related to time of use rates and load management. With regard to the other tariff revisions proposed by DEC, the Commission will accept them as recommended by the Hearing Examiner. (Unanimous.)

C. Code of Conduct

69. The parties have agreed that the Code of Conduct should be reviewed in a separate proceeding which, given the time constraints of this proceeding, appears to be an appropriate suggestion. We understand further that during the Code of Conduct proceeding, DEC will formally address both the appearance and the actual legal relationship between it and ODEC (Unanimous.)

D. Cost Accounting Manual

70. We accept the Hearing Examiner's recommendation that a review of the Cost Accounting Manual be conducted in tandem with the review of DEC's proposed Code of Conduct. (Unanimous.)

E. Supplier Agreement

71. Having sought clarification from DEC that the standards contained in the supplier agreement are consistent with those that the Commission has previously approved for DP&L, we adopt DEC's proposed supplier agreement with the understanding that no impediments will be put in the way of Commission-approved suppliers being able to compete for the Cooperative's customers. (Unanimous.)

F. Integrated Resource Plan

72. We believe DEC's proposal to be reasonable and, as this issue was not disputed, we agree to terminate the IRP requirements imposed by PSC Regulation Docket No. 35 and require DEC to file an annual report similar to that required of Delmarva. (Unanimous.)

G. Process Issues

73. The Settlement Agreement made between Staff and DEC was attached to the Hearing Examiner's report to apprise the Commission of the issues being discussed among the parties. The majority of these issues are not disputed. Resolution of issues by settlement is promoted by both the Public Utilities Act and the Restructuring Act. (26 *Del.C.* §§ 512 (a) and 1015(b).) Moreover, the Commission is authorized to approve settlements if they are in the public interest (even if all parties are not in agreement). (26 *Del.C.* § 512(c).) Noting that this Settlement Agreement is with prejudice, however, we adopt the resolution of these issues without prejudice. We also note that if over time any party to this proceeding feels that the issues as resolved are not functioning as intended, any party may resubmit such issues to the Commission. Specifically, since the DPA was not part of the Settlement Agreement, if the DPA is not satisfied with the resolution of any issues, it may resubmit such issues to the Commission for further consideration. (Unanimous.)

74. For the process issues of Customer Education, Phase-in and Notification, Supplier Switching, Supplier Withdrawal, Physical Connection/Disconnection, Load Profiling, Dispute Resolution and Supplier Interaction Protocols/Electronic Data Exchange, we find the Hearing Examiner's recommendation on these issues reasonable and adopt his findings on these process issues. (Unanimous.)

75. The process issue of Enrollment presented some dispute, centering on the appropriateness of the $4.75 charge. DEC clarified for the Commission that the Settlement Agreement addresses this issue. Specifically, DEC agreed to mail enrollment packages one time without charge at a customer/member's request and that subsequent package requests will be subject to a $4.75 charge. While cognizant that DEC will incur costs involved in the enrollment process, all parties must bear in mind that the goal of retail competition is for the customer to participate. For the sake of clarity, we adopt the Hearing Examiner's recommendation, as stated in the Hearing Examiner's Report recommending approval of the settlement that allows customers to receive enrollment packages one time without charge and thereafter at a charge of $4.75. Further, we require DEC to provide to customers upon request, customer usage data free once a year. (Unanimous.)

76. For the process issue of Metering and Billing, we find DEC's 6-step billing proposal to be reasonable. Further, we find DEC's stated purpose of the process - to ensure that customer/members are billed appropriately under retail competition and that bills are properly posted - to comport with the spirit of the Act. Thus, we adopt DEC's proposal, but with the understanding that the billing format will be reviewed with Staff prior to implementation. (Unanimous.)

77. As to the Balancing and Settlement process issue, we adopt the Hearing Examiner's recommendation, but only with the understanding that DEC is itself responsible for accomplishing balancing and settlement. If DEC elects to subcontract these matters to ODEC, that is DEC's exclusive decision. However, the Commission and all interested customers and parties, must be able to hold DEC accountable for performance. We, therefore, require DEC to promptly provide the proposed procedure to Staff and the other DPRC parties for their review and comment. (Unanimous.)

H. Customer Retention and "Gaming"

78. DEC has expended considerable effort in warning of the perils it faces from customer "gaming." DEC, has however, failed to demonstrate the manifestation of this fear through any supportable evidence. DEC disputes Staff's suggestion that the retention period applied to Delmarva be applied to DEC. DEC has maintained that the difficulty in applying the Delmarva retention period to DEC is that while 54% of Delmarva's load is protected under that application, only

4% of DEC's load is protected, since the majority of DEC's customer/members are served in the residential class. Thus, DEC has argued the predominant prospective culprits will be "residential gamers." DEC's last contention as to why it is vulnerable is because unlike Delmarva, DEC is a cooperative with no shareholders to absorb uncollected costs. The DPA claims that there has been no evidence by DEC to support the claim for gaming. While we understand the DPA's opposition to the imposition of any retention period, we adopt the Hearing Examiner's recommendation that no retention period should apply to those customers with monthly peaks under 300 kW and for those customers with monthly peak loads of 300 kW or above, a 12-month retention period shall apply. Our reasoning for this adoption is that first, we wish to protect DEC's small customer/members from such financial incursions. Second, we believe that DEC's larger customers will actually have more incentive to game the system, as well as the greater ability to do so, than will DEC's residential customers. (Unanimous.)

I. Rate Unbundling

79. The parties have all expended great amounts of time and energy in defending their positions on this matter. At issue is a debate over methodology. To review, DEC claims its proposal complies with the Commission's previous ruling on rate unbundling and that the methodology is dictated by the Act, which states that rates are to be frozen. DEC seeks to make its distribution charges the residual in calculating the components of the unbundled base rate, stating that to do so is consistent with the Act. Staff maintains that we should follow the methodology set forth in the Delmarva proceeding, where the distribution rates are kept constant throughout the transition period.

80. We read the Act as not requiring the calculation of either fixed or residual components in the unbundling process. In addition we believe that the Delmarva case is not good precedent since it was partially settled and, in this proceeding, much has been written and argued concerning the proper way to unbundle DEC's rates and comply with the Act. Our resolution of the proper way to unbundle DEC's rate is set forth below in our discussion of shopping credits.

J. Retail Market Price/"Shopping Credit"

81. This too is an issue upon which all the parties have spent enormous effort. DEC interpreted the Act to require that the retail market price be based on wholesale electricity market prices, suggesting that if the market price rises, the shopping credit should rise so that customers have a real opportunity in the market place. Staff's proposed methodology determines the shopping credit as a residual component after the other unbundled elements of the base rates have been set. DPA believes the shopping credit should include both wholesale electric price and a reasonable allowance for retail margin.

82. We find that DEC's case is less complex than the Delmarva case because DEC has traditionally had distribution charges set by the Commission. Additionally, DEC's cost of power is passed through to its customers under its purchase power contract with ODEC. Further, it should be noted that when the Commission set DEC's distribution rates, those rates included a certain level of margin. Thus, the claim that DEC "sells at cost" is not true since margins by definition are not costs. Thus, the difference between DEC and a stockholder organization centers on what is done with the profit/ margin, not on the mistaken belief that as a cooperative DEC only recovers its costs and no more.

83. In looking at the calculation of the average residential unbundled rate, it is clear that the rate needs to be divided into distribution, transmission, ancillary services, shopping credits, and CTC components. Given the legislative requirement that DEC's rates remain frozen during the transition period, it is clear that even if it is anticipated that market rates for electric power may rise during the next five years, that the costs of operating a distribution system are likewise not going to go down. Thus, Staff's approach of using the same value for each component, once determined, for the entire transition period appears to be the fairest resolution of an inherent conflict that all components of the rate structure cannot rise and still maintain the same level of rates. This appears to be an appropriate balance between the reality of the market place and the legislative directive that DEC's rates should remain frozen for the next five years. It is also

consistent with the approach adopted in the Delmarva proceeding which disaggregated the rates and then reviewed the components on an individual basis to determine the appropriate levels consistent with the legislative mandate that the rates remain frozen throughout the transition period.

84. In addition to Staff's proposed unbundled rates, DPA's suggestion that some sort of adder should be included for retail margin is appropriate. In the breakdown of the rates, DPA suggested using $0.00226 which appears to the Commission to be a reasonable markup of the wholesale power costs for the purpose of establishing a retail adder and compares favorably to DEC's suggested retail adder of $0.0015. The rates attached to Order No. 5366 entered on February 28, 2000, comport with our decision on how best to unbundle DEC's rates. In the residential class, the bundled rate of $0.09144 should be divided as follows:

Distribution	$0.03346
Transmission	$0.00410
Ancillary Services	$0.00171
CTC	$0.00020
Shopping Credit	$0.05197

85. The residential shopping credit of $0.05197 reflects the addition of a retail adder of $0.00226 and a subtraction of a CTC of $0.00020. The shopping credit shall remain fixed throughout the five-year transition period except for a one time true-up for actual PCA costs for the year ended March 31, 2000. This will avoid the problem of having other portions of the rates changing during the transition period.

K. Reliability

86. There was no dispute over this issue and we adopt the Hearing Examiner's recommendation and accept DEC's proposals concerning the reliability standards. (Unanimous.)

L. Transition Costs

87. DEC claims that it will attempt to mitigate all of its transition costs, but to the extent that it is unable to do so, it requests that it be allowed to account for those costs on a deferred basis and collect them when it next files a base rate proceeding in 2004. Although no other party to the proceeding (other than DPA) objected to this proposal, we believe that the statute requires, and good regulatory policy suggests, that these costs not be deferred but, instead be collected over the transition period when they are likely to be incurred and, thereby, avoid the possibility of cross-subsidization. Thus, we find that DEC's one-time transition costs of $830,000 should not be deferred, but should be recovered through a uniform CTC charge which will be collected as part of the wires component of the unbundled rate for the five-year transition period. 26 *Del. C.* 1006(b)(1)(c); § 1007. With regard to the ongoing transition costs of $285,000 per year, we agree with the Hearing Examiner that these costs should be characterized as ongoing operational costs that are currently being recovered in existing rates, and for which no deferral is required. (Unanimous.)

M. Stranded Costs - SPI

88. This issue was the most contentious in the proceeding. In part, there is a general feeling by some of the parties and, in particular, the Commission, that DEC has not dealt candidly with certain aspects of this issue by not bringing the SPI plan to the attention of the Commission before now.

89. Regarding the calculation of stranded costs, it is clear that any estimate of stranded costs is only a proxy for how the market place would actually value certain assets. Since an actual sale of the assets is the only sure way to determine whether costs are stranded or not, and this Commission has determined in the earlier restructuring case involving Delmarva --and again here -- that divestiture is not what is appropriate, we are faced with making some sort of administrative determination on stranded costs. This requires the Commission to use estimates and testimony in the record as to the expected market value of DEC's share of stranded costs to determine the appropriate level of recovery in the transition period rates.

90. In the context of DEC's situation, where it has no actual generating facilities but is required by contractual agreement to take all of its electric needs from one supplier - ODEC -for an extended period of time, it is logical, as Staff and DPA pointed out, that the analysis should look beyond the transition period in order to determine what the appropriate value of stranded costs should be. In addition, in a competitive market DEC's customer/members will be able to choose from suppliers who can supply them through the PJM market place. Accordingly, from the stand point of DEC's customer/ members, the most appropriate comparison for determining stranded costs is PJM market rates, not VACAR pricing, since DEC's customers are located on the Delmarva Peninsula and in the PJM market. Considering all of the stranded costs calculations, the Hearing Examiner's conclusion, as well as the witness' testimony, the most credible estimates are that DEC has negative stranded costs whether VACAR market prices are used or PJM market prices are used. We estimate using VACAR market prices, that DEC has some $4 million in negative stranded costs, while the PJM market price comparison indicates negative stranded costs of $17 million. Since we have determined that the PJM market pricing is the most appropriate for purposes of establishing the level of stranded costs, we find that DEC has negative stranded costs of $17 million. In converting those negative stranded costs into a competitive transition charge (CTC), we find that the appropriate charge should be set at zero. Thus, we arrive at the same conclusion as the Hearing Examiner, which is that DEC's unbundled rates should reflect a zero value for stranded costs and that PJM prices are the appropriate prices upon which to calculate DEC's stranded costs. We find these conclusions to be the fairest outcome based on the record before us and, thus, we adopt it. (Unanimous.)

91. We now turn to the issue involving the SPI. The Commission has two distinct problems with the SPI issue. First, DEC and ODEC raise the issue that since the SPI is part of a rate filed under a FERC formula that this Commission is precluded from reviewing the appropriateness of the revenues collected under that formula. Putting aside the legal arguments, we find that there is serious question as to whether or not the SPI has been properly approved by FERC and what that means or implies for our jurisdiction. Second, DEC claims that the Commission had prior knowledge of the SPI. On this matter, there should be no dispute since DEC's contention is unfounded. Meeting with Staff members about a variety of issues, one of which may have involved discussing the SPI, does not constitute putting the Commission on notice with regard to its implementation, let alone suggest that the Commission somehow has *de facto* accepted it as an approved rate. Thus, the SPI comes to the Commission for the first time in this proceeding, almost two years after it was originally placed into the rates being charged DEC customers. Overall, the Commission believes DEC failed in its responsibility to inform the Commission of such a major change, especially given the effect on energy charges that DEC customers were being asked to pay.

92. However, notwithstanding our distaste at the position DEC has placed the Commission in (by not bringing this matter before us prior to now), the Commission does not accept the Hearing Examiner's recommendation suggesting that the SPI is an unauthorized rate. If the members are concerned about paying additional depreciation at an accelerated rate, causing customers to pay more for electricity than they otherwise might be required to pay, with retail competition these customers will have a choice to select an alternative supplier of energy and, thus, avoid this additional cost of supply. To the extent members are concerned about being charged in the past for rates that included the SPI, this is an issue for those members to take up with management and DEC's board of directors.

93. Because members will have a choice of electric suppliers going forward and the continuing right to elect directors and ultimately influence the management of the cooperative they own, we find it unnecessary to accept the Hearing Examiner's recommendation that the SPI should be discontinued forthwith and all such unauthorized amounts previously collected refunded to DEC's customers/members. In addition, we do not adopt the finding that DEC has no stranded costs since we had previously determined that in fact DEC does have negative stranded costs. (Unanimous.)

N. Miscellaneous

94. We adopt the remainder of the Hearing Examiner's Report that was not specifically addressed in our deliberations and which is attached to the original hereof and incorporated herein by reference as Exhibit "A."

IV. ORDER

AND NOW, this 25th day of April, 2000, for the reasons set forth herein, **IT IS HEREBY ORDERED:**

1. That Delaware Electric Cooperative, Inc.'s proposed restructuring plan, as amended herein, is approved.

2. The compliance rate filing shall be filed within fifteen days of the date of this Order, which shall include any necessary PCA adjustment for the twelve months ending March 31, 2000.

3. That the Commission's Order No. 5366, dated February 28, 2000, issued in this docket is incorporated herein by reference.

4. That no customer educational material should be disseminating prior to its review by the Consumer Education Working Group.

5. That the Commission terminates the IRP requirement imposed by PSC Regulation Docket No. 35 and, in lieu thereof, requires Delaware Electric Cooperative, Inc., to file an interim report similar to that required for Delmarva Power & Light in accordance with the approved partial settlement agreement of PSC Docket No. 99-163.

6. That the Hearing Examiner's Report attached to the original hereof as Exhibit "A" is accepted to the extent not specifically addressed herein.

7. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

*23 BY ORDER OF THE COMMISSION:

Chairman

/s/ Joshua M. Twilley

Vice Chairman

/s/ Arnetta McRae

Commissioner

/s/ John R. McClelland

Commissioner

Commissioner

ATTEST:

/s/ Karen J. Nickerson

Secretary

Footnotes

1 References to pre-filed direct testimony and other exhibits introduced at the evidentiary hearings will be cited as "Ex. ___ at ____." References to the parties' opening briefs to the Hearing Examiner will be cited as "[Party] at ____; references to reply briefs to the Hearing Examiner will be cited as """[Party] RB at ___;" references to briefs on exceptions to the Hearing Examiner's Report will be cited as "[Party] BOE at ____;" and the Hearing Examiner's Report will be cited as "HER at ___." Transcripts of proceedings will be cited as "Tr. at ___."

2 AFFECT is comprised of Delmarva/Conectiv, DEC, the Delaware Municipal Electric Corporation, the Low Income Electric Consumers Group, the Delaware Alliance of Alternative Energy Providers, the Delaware Energy Users Group, and ODEC. (HER at 7-8, footnote 6).

3 The Hearing Examiner disagreed with DPA's assertion that ODEC qualifies as an affiliate of DEC, since it fails to meet the PSC Regulation Docket No. 49 definition of "affiliate" (HER at 34.)

4 The proposed January 21, 2000 DPRC settlement addressed many of the enrollment issues raised by the parties during the proceedings.

5 DPA took exception to the Hearing Examiner's recommendation that a 12 month retention period apply to customers of 300 kW and above since DPA believes no retention period is appropriate for any customer irregardless of size.

6 PJM is an acronym for the PJM Interconnection Association which manages the wholesale bulk power grid in the mid-Atlantic region. "VACAR" is a similar association which manages the region consisting of Virginia and the Carolinas.

End of Document

TAB 4

2002 WL 1306032 (Del.P.S.C.), 217 P.U.R.4th 142

Re Delmarva Power and Light Company
Joint applicants: Conectiv Communications, Inc.; Potomac Electric Power Company; New RC, Inc.

PSC Docket No. 01-194
Order No. 5941

Delaware Public Service Commission

April 16, 2002

Before McRae, chair and Conaway, Puglisi and Lester, commissioners.

BY THE COMMISSION:

I. *BACKGROUND*

1. On May 11, 2001, applicants Delmarva Power & Light Company ('Delmarva '), Conectiv Communications, Inc. ('Conectiv'), Potomac Electric Power Company ('PEPCO'), and New RC, Inc., jointly filed an application ('Application') with the Public Service Commission of the State of Delaware (the 'Commission') for approval of the proposed transfer of indirect control of Delmarva and Conectiv to New RC and PEPCO via a merger of Delmarva's parent corporation, Conectiv, into a subsidiary of New RC. New RC is currently owned by PEPCO, but upon closing will become the parent of PEPCO and Conectiv.

2. The Commission opened this docket to consider the Application, and designated Robert P. Haynes as Hearing Examiner.

3. Besides Staff and the Division of the Public Advocate ('DPA'), the following parties intervened and participated in the proceedings: the International Brotherhood of Electrical Workers Local Union No. 1307 ('IBEW'); BOC Gases, Inc. ('BOC'); the Consumers Education & Protective Association of Delaware ('CEPA'); Mr. Bernard J. August ('Mr. August'); the Cable Telecommunications Association of MD, DE and DC ('Cable'); Old Dominion Electric Cooperative ('ODEC'), the Delaware Electric Cooperative ('DEC'); the Delaware Energy Users Group ('DEUG'); and AES NewEnergy, Inc. ('AES').

4. On October 17, 2001, Staff, ODEC/DEC, AES, and the DPA submitted direct testimony in opposition to the Application.

5. At Staff's request, the procedural schedule was suspended in order to permit the parties to engage in settlement discussions.

6. On November 28, 2001, a hearing was held at which all of the prefiled direct testimony was entered into the record, although cross-examination was adjourned to allow additional settlement negotiations.

7. On November 30, 2001, all parties except AES (the 'Settling Parties ') jointly filed a Proposed Settlement.

8. On December 14, 2001, AES filed supplemental direct testimony opposing the Proposed Settlement.

9. At a subsequent hearing to consider the Proposed Settlement held on December 18, 2001, AES's supplemental direct testimony was entered into the record, and the various witnesses supporting the Proposed Settlement testified orally in favor of the Proposed Settlement and were subject to cross-examination by AES.

10. On January 11 and 18, 2002, the Settling Parties and AES submitted initial and reply post-hearing briefs.

11. On February 12, 2002, the Hearing Examiner issued his Findings and Recommendations ('HER') in which he recommended that the Commission approve the Proposed Settlement in its entirety.

12. On February 26, 2002, AES filed exceptions to the HER that set forth the same objections to the Proposed Settlement as it had set forth in its supplemental direct testimony and post-hearing briefs. 13. The Commission met on March 19, 2002 to hear oral argument and to deliberate in public session with respect to the HER. This represents the Commission's final Findings, Opinion, and Order in this docket.

II. *FINDINGS AND OPINION*

*1 14. The Proposed Settlement is in the public interest and should be approved. We are mindful of AES's contentions in its exceptions to the HER, which contentions were also presented to the Hearing Examiner, but we believe that the Hearing Examiner correctly addressed those arguments and found them wanting. [1]

15. First, AES challenges the provision of the Proposed Settlement that establishes a rate freeze at the end of the Transition Period set forth in 26 *Del. C.* § 1004(a). AES asserts that the Proposed Settlement's rate freeze extends the Transition Period beyond that established in Section 1004(a). (AES Exceptions, page 2.) The Hearing Examiner dismissed this contention, finding that nothing in the Proposed Settlement extends the Transition Period beyond the dates provided in Section 1004, and noting that the Proposed Settlement actually recognizes the end of the statutory Transition Period because: (1) the rate freeze in the Proposed Settlement does not go into effect until after the Transition Period expires; and (2) the rates to be charged will be higher than the Transition Period rates. (HER at 26-27, ps 45.) We agree with the Hearing Examiner and adopt his reasoning.

16. Next, AES contends that the Proposed Settlement violates 26 *Del. C.* § 1006(a)(2) because there has been no showing that the post-transition rates will be representative of the 'regional wholesale electric market price plus a reasonable allowance for retail margin.' (AES Exceptions, page 2.) AES argues that none of the Settling Parties provided any 'evidence' of how the proposed rates were derived or that they comply with Section 1006(a)(2); rather, the Settling Parties only made 'mere oral assertions' that the proposed rates complied with Section 1006(a)(2). (*Id.* at 3.) AES further argues that this was not so, however, because the post-transition rates were derived in the 'exact same manner' as the transition rates and the fact that the proposed rates are higher than current transition rates does not mean that they satisfy the requirements of Section 1006(a)(2). (*Id.* at 5.) Thus, AES concluded, the Settling Parties have failed to meet their burden of proof with respect to the post-transition rates. (*Id.* at 3-5.)

17. The Hearing Examiner disagreed with AES's contentions. He found that Section 1006 did not change the Commission's authority to approve rate settlements when they were adequately supported and were in the public interest; rather, it only required the Commission to find that the proposed rates are 'representative of regional wholesale electric market prices, plus a reasonable allowance for retail margin.'' (HER at 30) (citation omitted in original.) The statute does not tell the Commission how it has to make that finding. Here, the Hearing Examiner accepted Staff's argument that the post-transition rates were calculated in the same way as the transition rates, and if the transition rates were acceptable, then the post-transition rates should be acceptable as well. (HER at 30, ps 52.) The Hearing Examiner also noted the testimony of Staff witness Dillard, Applicants' witness Wathen, and DPA witness Crane, each of whom concluded that the Proposed Settlement's rate provisions are reasonable and should be approved as consistent with Section 1006. The Hearing Examiner found that these witnesses provided sufficient supporting testimony that the Commission may reasonably rely upon in determining that the Proposed Settlement's rates are representative of the regional wholesale market electric price, plus a reasonable allowance for retail margin. (HER at 30, (ps 51.) Furthermore, the Hearing Examiner observed that settlements do not require the same evidence as a fully litigated case does; indeed, if AES's argument were to be accepted, no settlement could ever be supported 'if the parties had to agree on the 'correct' ratemaking recipe used to support the end result.' (*Id.*) Additionally, the Hearing Examiner pointed out that AES could have proffered its own evidence that the post-transition

rates did not comply with Section 1006(a)(2) but did not do so. (*Id.* at 30-31 (ps 53.) Finally, the Hearing Examiner observed that in a litigated rate case the Commission would have no authority to order Delmarva to freeze rates, and so the proposed rates should be considered as a benefit consistent with the public interest and Section 1006. (*Id.*)

18. We agree with the Hearing Examiner. This is a settlement of a contested proceeding, and under 26 *Del. C.* § 512 we need only determine whether the Proposed Settlement is in the public interest. We conclude that it is. The proposed rates were calculated in the same manner as the transition rates approved in PSC Docket No. 99-163, and the fact that those rates also were approved in a settlement is of no moment. The manner in which those rates were calculated was a contested issue at the hearing at which the proposed settlement of that docket was considered, and the Commission found that the rates did comply with Section 1006(a)(2). Therefore, we adopt the Hearing Examiner's reasoning in rejecting AES's contention.

19. On this same issue, AES argued that it had not had sufficient time to develop the record with respect to the rates in the Proposed Settlement. (AES Exceptions at 6.) The Hearing Examiner dismissed this contention, noting that AES could have (but did not) asked for discovery into the proposed rates at the time the procedural schedule was being revised to consider the Proposed Settlement; instead, it waited until the post-hearing briefing to raise the issue. In light of this, the Hearing Examiner concluded that AES had waived its argument concerning the lack of time to investigate the proposed rates. (HER at 32 ps 54.) We agree with the Hearing Examiner; if AES thought it needed additional time to investigate the proposed rates, it should have requested the Hearing Examiner to grant it that additional time, and if the Hearing Examiner declined to do so, it could have brought the matter before the Commission. Having failed to do so, it cannot now be heard to complain.

20. AES next takes issue with the Proposed Settlement's provision that it claims would change the 'returning customer' rule. Pursuant to Delmarva's current tariff, which we approved in connection with the settlement of PSC Docket No. 99-163, a large customer that returns to Delmarva's supply service from a competing supplier must either commit to remain with Delmarva for a 12-month period in exchange for a fixed price or it will be charged the monthly-changing Market Pricing Standard Service ('MPSS') without a 12-month commitment. The Proposed Settlement seeks to eliminate the fixed-price option, and to limit returning customers to either MPSS or a negotiated contract rate.

21. AES argues that the elimination of the fixed price option for returning large customers will 'present a formidable barrier to any customer contemplating participation in retail choice' because a customer that returns to Delmarva will be subject to potential spot market prices for several years under the MPSS tariff. (AES Exceptions at 7-8.) AES further asserts that this proposed change fails to comply with the requirements set forth in the Administrative Procedures Act for changing rules or regulations. (*Id.* at 7.)

22. The Hearing Examiner dismissed these contentions. First, he found that the proceeding in which the returning customer rule was first promulgated was a case decision, not a rulemaking procedure or procedure for implementing regulations. (HER at 35 ps 62.) He pointed out that the returning customer rule was part of Delmarva's tariff, and observed that in PSC Regulation Docket No. 49, the Commission had rejected attempts to make the returning customer provisions part of the regulations. Instead, the Commission ordered that customer retention issues be handled individually for each utility. (*Id.* at 36 ps 63.)

23. The Hearing Examiner next turned to AES's argument that a returning customer is entitled to standard offer service under Section 1006, which he found had 'some merit.' (*Id.* at 37 ps 65.) However, the Hearing Examiner was persuaded by Staff's argument that the Commission could determine different rates for different customers based upon different usage, noting that the transition period rates were different for each rate class. The Hearing Examiner observed that under the Act's definition of standard offer service, a returning customer was entitled to standard offer service, but nothing mandated that a returning customer receive the same standard offer service as other customers [that never left]. (*Id.*) The Hearing Examiner rejected AES's argument that standard offer service rates must be fixed, noting that market prices are not fixed and that it was reasonable for the Commission to conclude that the flexible rate in MPSS was appropriate as the standard offer service rate for large customers who are particularly responsive to market

prices. (*Id.* at 37 ps 66.) The Hearing Examiner also pointed out that in PSC Docket No. 99-163 the Commission had recognized that returning customers could impose higher costs and respond to market conditions and competition more quickly than other customers, and that Section 1010(c) of the Act supported retail market price rates for larger customers that might be higher than the standard offer service rates available to other customers. (*Id.* at 38 ps 67-68.)

24. We agree with and adopt the Hearing Examiner's reasoning in rejecting AES's contentions with respect to the returning customer rule.

25. AES next argues that the Proposed Settlement's methodology for correcting the inadequacies in the transmission system has numerous weaknesses, and those weaknesses require the formation of a working group to provide 'constructive, concrete feedback' to the Commission. (AES Exceptions at 8-9.) The Hearing Examiner agreed with the Settling Parties that the Proposed Settlement adequately addresses the transmission congestion issue raised by ODEC/DEC and Staff, and further noted that the settlement negotiation process itself constituted a 'working group' of the sort sought by AES. Furthermore, the Hearing Examiner opined that the Proposed Settlement's mechanism should be implemented and monitored before the Commission intervened to impose any additional steps. Finally, the Hearing Examiner observed that the Commission currently had an open rulemaking docket concerning reliability in which the transmission issue could be pursued further. (*Id.* at 42-43, ps 76-79.)

26. Again, we agree with and adopt the Hearing Examiner's conclusions and recommendations on this issue. We are sympathetic to AES's concerns, but we believe that the process set forth in the Proposed Settlement is reasonable and should be given an opportunity to work. If a party believes that the process set forth in the Proposed Settlement is not working, that party is free to bring its concerns before the Commission.

*2 27. Finally, AES asserts that the Hearing Examiner's conclusion that the Proposed Settlement benefits competition as a whole 'fails to recognize that MPSS service is no longer an option, but a mandatory [standard offer service] upon return to utility [standard offer service] for large customers (other than an unspecified negotiated contract option).' (AES Exceptions at 9.) Rather, AES contends, the Proposed Settlement will result in the continuation of monopoly standard offer service to retail customers through May 1, 2006, which is detrimental, not beneficial, to competition.

28. We disagree that the Proposed Settlement is detrimental to competition. We do not believe, for example, that it is in the public interest to abandon a cap on how high rates can go in order to encourage more competition and possibly have Delaware consumers pay even higher rates. But even if the Proposed Settlement did not promote competition, the promotion of competition is not the sole issue that we should consider in determining whether the Proposed Settlement is in the public interest. We are convinced that the Proposed Settlement is in the public interest because, among other things (and in addition to the rate freeze):

• it maintains Delmarva's operational headquarters and significant senior management in Delaware for the next five years (thus maintaining jobs for Delaware residents);

• Delmarva will maintain its current level of charitable contributions;

• Delmarva will not seek rate recovery of merger-related costs (which are frequently substantial, and we have no reason to believe the same is not true here);

• Delmarva will contribute $200,000 to an organization designated by Staff and the DPA for the promotion of renewable resources in Delaware and for informing customers of such organization;

• Delmarva will adopt service level guarantees for keeping appointments, installations for new residential customers, bill accuracy and outage restorations, and other service level guarantees will be addressed in other separate proceedings;

• Delmarva will add three transmission projects to be completed by May 2008 and will accelerate one already-planned transmission improvement for completion by May 2006;

• Delmarva will make a $750,000 contribution to Murex Investments in a form that will trigger matching federal or state funds, to the extent that such funds are available and conditioned upon spending the funds on job training and small business development within Delmarva's Delaware service territory;

• Delmarva would implement a methodology designed to lower the congestion over its transmission system through using analysis of 'off-cost operations' data available from PJM;

• The Applicants agreed to honor all union contracts relating to severance and benefits and to engage in future good faith negotiations, consistent with the requirements of 26 *Del. C.* § 1016(b);

*3 • Delmarva agreed to make modifications with respect to information exchanges with competitive suppliers and in its peak management program, which addresses the issues initially raised by AES in its direct testimony and identified by AES as changes that would promote the development of competitive electricity markets; and

• Each Settling Party retains the right to petition the Commission to reopen this proceeding for the purpose of substituting the terms and conditions of this Settlement with the terms and conditions of a different settlement if entered into by Delmarva in Maryland. Such right shall be exercisable only within 30 days of the filing of such settlement made in Maryland.

29. These are very real benefits to the residents of the state of Delaware, and these benefits accrue to all groups, not simply the providers of energy. We find it significant that groups with interests as diverse as DEUG (large industrial users which support customer choice and competition) and CEPA (which started out opposed to the merger) support this settlement, which suggests that they find benefits to their own constituencies in the Proposed Settlement. That having been said, we believe that AES played a very valuable role in this proceeding in bringing issues to the Commission for consideration, even if we ultimately rejected those arguments.

30. Turning to the approval of the merger, we find that the proposed merger satisfies 26 *Del. C.* § 215(d) in that it is in accordance with law, is for a proper purpose, and is consistent with the public interest. The record reflects that the merger will enhance reliability through increased investment strength. It will enhance customer service through the service guarantees adopted in the Proposed Settlement, and the service guarantees to be considered in separate proceedings. There are also potential benefits associated with size, such as economies of scale in connection with purchasing (Exhs. 2-4 (testimony of Delmarva witnesses)). We also find that the proposed merger satisfies the requirements of 26 *Del. C.* § 1016(a) that any proposed merger insure that the successor will continue safe and reliable transmission and distribution services. The record shows that with the improvements to Delmarva facilities that will be made over the course of the next few years, PEPCO is committed to maintaining a high level of service to Delaware customers. The proposed merger meets the requirements of 26 *Del. C.* § 1016(b) as well, relating to commitments made regarding existing collective bargaining agreements and future negotiations with collective bargaining units.

ORDER

AND NOW, this 16th day of April, 2002, *IT IS HEREBY ORDERED*:

1. That the Hearing Examiner's Findings and Recommendations attached hereto as Exhibit 'A' are adopted in their entirety.

*4 2. That the merger among Delmarva Power & Light Company, Conectiv Communications, Inc., Potomac Electric Power Company, and New RC, Inc., is hereby approved.

3. That the Commission reserves jurisdiction and authority to enter such further orders in this matter as may be deemed necessary or proper.

EXHIBIT 'A'

FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

Robert P. Haynes, duly appointed Hearing Examiner in this Docket pursuant to 26 *Del. C.* § 502 and 29 *Del. C.* Ch. 101, by Commission Order No. 5722, dated May 22, 2001, reports to the Commission as follows:

I. APPEARANCES

The following counsel and pro se parties appeared at the hearings:

On behalf of Delmarva Power & Light Company d/b/a Conectiv Power Delivery: BY: RANDALL V. GRIFFIN, ESQUIRE. On behalf of Potomac Electric Power Company: BY: KIRK EMGE, ESQUIRE. On behalf of the Public Service Commission Staff: ASHBY & GEDDES, BY: JAMES McC. GEDDES, ESQUIRE. On behalf of the Division of the Public Advocate: BY: G. Arthur Padmore, Public Advocate. On behalf of Delaware Electric Cooperative, Inc. and Old Dominion Electric Cooperative, Inc.. LeCLAIR RYAN, P.C., BY: ERIC M. PAGE, ESQUIRE. On behalf of Delaware Energy Users Group: CHRISTIAN & BARTON, L.L.P., BY: LOUIS R. MONACELL, ESQUIRE. On behalf of BOC Gases: McNEES, WALLACE & NURICK, BY: DAVID M. KLEPPINGER, ESQUIRE, SUSAN M. BRUCE, ESQUIRE. On behalf of AES New Energy, Inc.: ALEXANDER & CLEAVER, P.A., BY: CHANTEL R. ORNSTEIN, ESQUIRE, BERNARD J. AUGUST, PRO SE.

II. PROCEDURAL HISTORY

1. On May 11, 2001, Applicants Delmarva Power & Light Company ('Delmarva' or 'DP&L'), Conectiv Communications, Inc. ('CCI'),[2] Potomac Electric Power Company ('Pepco') and New RC, Inc. jointly filed an application ('Application ') with the Public Service Commission of the State of Delaware ('Commission ') for approval of the proposed transfer of indirect control of Delmarva and CCI to New RC and Pepco via a merger of Delmarva's parent corporation, Conectiv, into New RC, which is owned by Pepco. The filing was made pursuant to sections 215 and 1016 of the Public Utilities Act of 1974, as amended. 26 *Del. C.* §§ 215 and 1016.

2. On May 22, 2001, in Order No. 5722, the Commission established this proceeding, assigned the matter to this Hearing Examiner, and directed public notice be published of the Application and the Commission proceeding. Ex. 1.

3. A pre-hearing conference and public comment hearing was held in Dover on June 18, 2001, and additional public comment hearings were held the evenings of September 10, 12, and 18, 2001, in Wilmington, Dover, and Georgetown, respectively.

4. The parties to this case are the Applicants, the Commission Staff ('Staff '), the Division of the Public Advocate ('DPA'), the International Brotherhood of Electrical Workers Local Union 1307 ('IBEW'), BOC Gases ('BOC'), the Consumers Education & Protective Association of Delaware ('CEPA'), Mr. Bernard J. August, the Cable Telecommunications Association of MD, DE & DC, Old Dominion Electric Cooperative ('ODEC'), Delaware Electric Cooperative ('DEC '), the Delaware Energy Users Group ('DEUG'), and AES NewEnergy, Inc. ('AES').

5. On October 17, 2001, Staff, DEC/ ODEC, DPA, and AES submitted prepared direct testimony in opposition to the Application. Prior to the filing of Applicants' rebuttal testimony, Staff requested suspending the procedural schedule except for the scheduled hearing on November 28, 2001. This request was made to allow settlement discussions, and it was granted, as it was not opposed, although the parties were directed to continue with their discovery.

6. On November 28, 2001, a hearing was held in Dover at which time the parties' direct testimonies were admitted into the record, with cross-examination deferred until a later date. At the request of the parties, the hearing was adjourned to allow further settlement negotiations. Following the settlement conference, the parties reported that a settlement would be submitted on behalf of most of the parties, and they presented a revised procedural schedule in order to review the settlement and any opposition to it. This revised schedule was approved without objection.

7. Pursuant to the schedule, on November 30, 2001, Applicants, Staff, DPA, BOC, CEPA, DEC, ODEC, IBEW, Bernard August and DEUG (hereinafter jointly referred to as 'settling parties') jointly filed a document entitled 'Proposed Settlement.' On December 14, 2001, AES filed supplemental direct testimony in opposition to the Proposed Settlement, and this testimony and the oral testimony supporting the Proposed Settlement by Applicants, Staff, DPA and DEC/ ODEC witnesses were received into evidence on December 18, 2001 at a duly noticed technical public hearing held in Wilmington. Ex. 15. A further duly noticed public comment hearing was held in Dover on December 20, 2001. *Id.*

8. On January 11, 2002, Applicants, Staff, DPA, DEC/ODEC, BOC, DEUG, and AES submitted initial post-hearing briefs, and on January 18, 2002, Applicants, Staff, DPA, DEC/ ODEC, DEUG, and AES submitted reply briefs. IBEW also submitted a late reply brief.

9. The evidentiary record consists of twenty exhibits, 363 pages of verbatim transcripts, and public oral and written comments. I have considered the entire record and the arguments in the post-hearing briefs,[3] and submit for the Commission's consideration these Findings and Recommendations.

III. SUMMARY OF THE EVIDENCE[4]

A. Applicants

10. Applicants' direct case consisted of three statements of pre-filed testimony submitted by five witnesses. Pepco Chairman and Chief Executive Officer John M. Derrick, Jr. and Conectiv President and Chief Operating Officer Thomas S. Shaw jointly testified to the merger's general benefits. Ex. 2. They noted that the merger would result in the combined utilities being the largest electric delivery company within PJM, with 1.8 million customers in Delaware, New Jersey, Maryland, Virginia, and the District of Columbia. Ex. 2 at 3. They explained that the credit quality of the companies would continue to be strong, with investment-grade securities, and that future operations of Conectiv and Delmarva would be largely unchanged, remaining as separate companies, headquartered in Delaware, known by the same names and staffed by substantially the same employees. *Id.* at 4, 13-14.

11. Witnesses Derrick and Shaw described the reasons for the merger, and detailed its expected benefits for both shareholders and customers. They cited enhancing both reliability through increased investment strength, and customer service through a continued focus on service and a set of customer service guarantees. *Id.* at 7-8. Their testimony also noted the potential future benefits of a larger organization that would be better situated to coordinate customer service activities, to identify and implement 'best practices' and to capture cost-effective benefits of new technologies. *Id.* at 9-10, 12-13. Messrs. Derrick and Shaw explained that there would likely be cost savings over time, but that there 'are no substantial immediate rate reduction opportunities' because the 'benefit of maintaining separate, stand-alone operating companies' also means that there 'will be few, if any involuntary terminations.' *Id.* at 10-11. The witnesses committed Applicants to honoring all union contracts after the merger and to engage in good faith bargaining in future negotiations. *Id.* at 11.

12. The Applicants presented Dr. Joe D. Pace, an economist and director of LECG, LLC, a consulting firm. Ex. 3. Dr. Pace testified that the increased size of the Applicants after the merger will provide the companies with the added scale and greater depth to meet the future challenges in a restructured industry. Ex. 3 at 6. He described that the Applicants would integrate their functions selectively once the merger is consummated and that such integration would benefit customers through performance improvements and the implementation of 'best practices'E, 217 P.U.R.4th 153>>practices' without increasing costs. *Id.* at 10-11. Dr. Pace gave examples of how the benefits of a larger, more diverse organization can improve customer service, better respond to emergencies, reduce purchasing costs, and respond to technological and structural changes. *Id.* at 11-17. Dr. Pace also testified that the increased scale of the merged organization could help the companies meet the challenges that could be posed in the event that Delmarva remained the default supplier after the transition period. *Id.* at 24-25. He noted that supply procurement strategies in the future would rely far more heavily on sophisticated buying and financial risk hedging strategies than when a utility relied primarily on its own generation plants and long-term contracts for its energy supply requirements. *Id.*

13. Applicants presented the direct testimony by Derek W. HasBrouck, an Associate Partner of PA Consulting Group, P.A., who set forth the Applicants' proposed customer service level guarantees. Ex. 4. Mr. HasBrouck testified that Applicants offered the guarantees as a benefit of the merger and at no cost to ratepayers. *Id.* at 8. Mr. HasBrouck's testimony explained how the Applicants selected these particular guarantees, and commented 'few utilities in the U.S. have committed to a comprehensive package of guarantees that matches the Companies' proposal.'*Id.* at 9, 18. The package includes: a) an Appointments Met guarantee where Delmarva would pay a customer $25 if the Company failed to honor a mutually agreed face-to-face appointment; b) a New Connections guarantee where Delmarva would pay $100 to a residential electric or gas customer whose property was ready for service to be installed, if Delmarva failed to do so within 10 days; c) a Residential Bill Accuracy guarantee where Delmarva would provide a $5 credit for all customers affected for a mistake on the utility portion of the total utility charge if the customer brought the mistake to the Company's attention; d) an Outage Restoration guarantee where a $25 credit would be paid to a customer whose service is interrupted for more than 24 hours; e) a Call Center Telephone Service Factor commitment by the Applicants to answer 70% of all calls to their call centers within 30 seconds; f) a Call Abandonment commitment so that no more than 5% of customers 'in queue' waiting for a service representative abandon their call before reaching such a representative; g) an Individual Poor Performing Circuit Guarantee, committing that action plans will be developed to ensure that no circuit will be on a list of the poorest 2% of circuits for more than two years in a row; and h) and i) Reliability commitments made to guarantee that Delmarva's Customer Average Interruption Duration Index ('CAIDI ') and System Average Interruption Frequency Index ('SAIFI') do not exceed two standard deviations above their historical mean. *Id.* at 11-15.

14. Each of the proposed service level guarantees has certain limitations, exclusions and conditions. Ex. 2, Sch. DWH-3. Mr. HasBrouck testified that these guarantees 'represent a strong commitment by the Companies to maintain or enhance customer service and reliability after the completion of the proposed merger' and that these guarantees provide benefits to customers, either directly through credits or indirectly by focusing the Applicants' attention on the customer and provide quality, consistent and cost-effective service that customers deserve. *Id.* at 19.

15. At the hearing on December 18, 2001, oral testimony in support of the Proposed Settlement was presented by Applicants' witnesses Joseph Mack Wathen, Conectiv's Director of Planning, Finance and Regulation, and Jerry A. Elliott, Conectiv's Director of Transmission and Distribution System Reliability. Mr. Wathen described the Proposed Settlement's main terms and testified that it, as a whole, was in the public interest and should be approved. Tr. 229 If the Proposed Settlement is approved, he concluded, then the merger would be for a proper purpose in accordance with law and consistent with the public interest, and Delmarva would continue to provide safe and reliable transmission and distribution services after the merger. Tr. 230. He also stated that the Proposed Settlement satisfied the organized labor requirements of Section 1016. Mr. Wathen further testified that the Proposed Settlement will promote competition by increasing the shopping credits, changing tariff provisions on peak management in order to facilitate the exchange of information between Delmarva and

competing suppliers, and using the fluctuating monthly Market Priced Supply Service rates, as opposed to allowing a large returning customer to receive Standard Offer Service ('SOS') fixed rates for twelve months. Tr. 230-31.

16. Mr. Elliott testified on the Proposed Settlement's provisions on reliability and congestion, and specifically addressed the concerns raised by the Staff's witness, Dr. Glover. Mr. Elliott concluded that the transmission system would maintain its reliability and meet all applicable transmission reliability criteria if Delmarva followed its current construction plans and completed three additional projects, which the Proposed Settlement would require. Tr. 282-83. Mr. Elliott also described the Proposed Settlement's mechanisms to attempt to resolve the congestion issues in the proceeding, and he stated that the Proposed Settlement specifies that certain additional construction projects will be completed by Delmarva or by ODEC. Tr. 283-84. He further described the mechanism that will address congestion issues on an ongoing basis through least-cost analyses, which are triggered by specified amounts of congestion. Tr. 285. The trigger congestion levels are higher in the earlier years of the Proposed Settlement, and thereafter would be reduced until May 2006 when the Proposed Settlement ends. Mr. Elliott concluded that these provisions, in conjunction with the rest of the Proposed Settlement's provisions, are in the public interest. Tr. 286.

B. Staff

17. Staff presented the pre-filed testimony of three witnesses, John Stutz, Ph.D., a Vice-President of Tellus Institute, a consulting firm, J. Duncan Glover, Ph.D., P.E., Principal Engineer at Exponent Failure Analysis Associates, a consulting firm, and Janis Dillard, Regulatory Policy Administrator.

18. Dr. Stutz recommended that the proposed merger either be rejected or approved with conditions that would improve customer service and reliability. Ex. 13, Ex. 13A. His major points were: a) the Applicants' merger proposal does not guarantee any ratepayer benefits, such as a reduction in rates, or any improvement in service quality or reliability; b) the merger-related savings that the Applicants identify, if they are fully realized, would provide minuscule benefits to ratepayers; and c) the financial pressure on Pepco to obtain a return on its investment in the acquisition will create a financial incentive for actions that could increase the cost of electricity, and could adversely affect the quality of service and reliability to Delmarva's ratepayers.

19. Dr. Glover presented testimony on Delmarva's transmission planning, transmission reliability, and transmission congestion, and he supervised several power-flow analyses related to these issues. Ex. 11. Dr. Glover recommended: a) that all of the currently planned transmission upgrades in Delmarva's planning documents be completed by their existing in-service dates, as modified by the accelerated dates he recommended; b) that the in-service date of the proposed 230 kV line from Red Lion to Milford to Indian River should be advanced to June 10, 2005; c) that any proposed changes to Delmarva's transmission plan should be reported to Staff at least 12 months in advance; d) that the Commission should encourage Delmarva to procure additional rights-of-way for new, future transmission construction on and into the Peninsula and conduct long-term planning to ensure adequate transmission reliability; e) that two upgrades to the Hallwood-Oak Hall 69 kV line should be undertaken to alleviate congestion; f) that Delmarva study ways to alleviate the economic impacts of congestion associated with the Indian River AT-20 autotransformer; and g) that Delmarva adopt a proposed congestion alleviation mechanism. Dr. Glover's proposed congestion alleviation mechanism would require Delmarva to evaluate the economic impacts of congestion when it exceeded a certain threshold, and to determine the transmission projects needed to alleviate the congestion. Under this mechanism, the congestion charges paid by all load-serving entities would be compared with the costs of the transmission projects. Dr. Glover recommended that Delmarva undertake the transmission projects that were found to be economically feasible in order to relieve the congestion.

20. Ms. Dillard testified on the lack of symmetry between the potential risks and potential benefits of the proposed merger, with the potential risks outweighing the potential benefits. Ex. 12. She described the potential risks as including a decline in customer service and reliability, continuing higher energy prices on the Delmarva Peninsula resulting from transmission congestion and high market concentration, and the potential for market power abuse from Conectiv's mid-merit generating unit strategy. She sponsored Staff's recommendations, which were that the Commission reject the merger or approve the merger if certain tangible benefits from the merger were guaranteed.

She also summarized the merger conditions that Staff recommended, as follows: a) extending the rate cap on the supply component of rates; b) completing transmission upgrades to improve reliability and allow access to generating resources; c) adopting a dynamic mechanism to alleviate transmission congestion; d) adopting recommendations regarding long-term reliability and import capability on the Peninsula; e) strengthening proposed customer service guarantees and reliability standards; f) implementing a new customer bill credit applicable to the worst performing distribution circuits; g) adopting a financial incentive mechanism as a protection against the potential for a decline in customer service and reliability; h) barring current or future collection of merger costs or merger-related termination costs; and i) considering a requirement for DP&L to include a component of renewable supply in the choices it offers customers.

21. Ms. Dillard also presented oral testimony in support of the Proposed Settlement in which she explained its benefits to ratepayers.

C. DPA

22. DPA presented the prepared direct testimony of Andrea C. Crane, Vice-President of the Columbia Group, a consulting firm. Ex. 10. Ms. Crane's testimony made the following conclusions and recommendations: a) the merger is being undertaken for competitive positioning as we enter a new era of electric deregulation; b) in evaluating the merger, the Commission must recognize that the merger is being driven by the needs of management and shareholders, not electric ratepayers; c) utility management will benefit handsomely from this merger; d) efforts to date at deregulation have proven ineffective throughout much of the utility industry, and have been particularly disappointing in Delaware; e) the proposed merger could effectively eliminate one potential competitor from the State; f) there are likely to be cost savings as a result of this merger; g) as a matter of policy, cost savings resulting from utility mergers should be passed along to ratepayers; h) given that rates are frozen in Delaware, merger savings cannot be flowed through to ratepayers through an immediate rate reduction, but several other actions are recommended that can provide benefits to ratepayers and ensure that they receive a fair share of merger benefits; i) the Commission should condition its approval of the merger upon the commitment of DPL to continue to offer a bundled standard offer service in Delaware at present rates through December 31, 2006; j) all costs to achieve the merger should be paid for by shareholders and not allocated to the Applicants' ratepayers; k) the Commission should order that no acquisition premium relating to the merger would be collected in future regulated utility rates; l) utility companies should not need to receive incentives in order to provide acceptable service; and utilities should not be rewarded for providing service above certain defined acceptable levels; m) it is important to review customer service and reliability issues in order to ensure that adequate levels of customer service and service reliability will be maintained after the merger; n) Delmarva appointments that are missed or cancelled on less than 48 hour notice should be subject to a $100 penalty, unless an appointment is cancelled due to weather and the customer is promptly notified; o) the Applicants' guarantees with regard to service connections should be extended to commercial and industrial customers, who should receive a credit of 50% of one month's service if the connection is not provided within 10 days; p) the Applicants' guarantee for billing accuracy should be extended to commercial and industrial customers and a credit of $100 should be given for each bill that is in error; q) the Applicants' guarantee with regard to the call center service level and call abandonment rate should be addressed in PSC Docket No. 99-328; r) the service restoration guarantee credit should be given for each 24-hour period that the customer is without service; s) the definition of 'major event' should be revised to eliminate certain actions that should be within the Applicants' control; t) the outage guarantees (CAIDI and SAIFI) and the individual circuit performance guarantee should be addressed in PSC Docket No. 50; u) the Commission should retain jurisdiction over all corporate allocations; v) the Commission should require Conectiv to file a revised cost allocation manual prior to Conectiv Resource Partners or other Conectiv affiliates providing any services to Pepco or to Pepco affiliates; w) the merger should be conditioned upon the retention of the Conectiv headquarters in Delaware through December 31, 2006; and x) Conectiv's shareholders should be required to make contributions of $100,000 per year to the Environmental Incentive Fund through December 31, 2006. Ex. 10 at 3-5.

23. In addition, Ms. Crane provided oral testimony in support of the Proposed Settlement, which she concluded provides several benefits that are crucial not only to all ratepayers, but also to enhancing the evolution of a competitive electricity market in Delaware. Tr. at 291-95. Foremost among these benefits,

Ms. Crane noted, is the Proposed Settlement's provisions that places a rate freeze on Delmarva's rates for its distribution, transmission, and ancillary services beginning from the end of the current transition period through May 1, 2006, except for limited exceptions. *Id.* In addition, she testified that the Proposed Settlement also provides ratepayers with a reasonable assurance that the level of rates associated with SOS supply will remain stable through May 1, 2006 at a level 3% higher than the current transition period's rates. *Id.* at 290.

24. Ms. Crane also pointed out that the Proposed Settlement assures that Delaware ratepayers will not have to pay any of the costs associated with the merger, including not only the acquisition premium, but also transaction costs and termination fees. *Id.* at 292. In addition, Ms. Crane testified, that the Proposed Settlement provides tangible service guarantees to ratepayers with respect to appointments kept, new customer installations, residential bill accuracy, and outages. *Id.*

25. Ms. Crane also pointed out that with respect to large customers, the Proposed Settlement resolves several problems affecting Delmarva's largest customers, and it commits Delmarva to implement certain transmission system upgrades, which will enhance reliability and, thus, benefit all ratepayers. *Id.* at 292-293.

D. DEC/ODEC

26. DEC and ODEC jointly presented the direct testimony of four witnesses. DEC/ ODEC's first witness, J. William Andrew, Vice President, Engineering & Operations Division for DEC, testified about the impacts of transmission congestion costs on DEC and its members. Ex. 5. Mr. Andrew explained that congestion charges incurred by ODEC are passed through to DEC and other member cooperatives. He then described the severe financial impact of the congestion charges recently incurred by DEC and ODEC. Mr. Andrew warned that unless there is relief from transmission congestion, all electric consumers in the State of Delaware would suffer. He then commented on additional transmission improvements on the Delmarva system necessary to reduce congestion and the extreme cost penalties imposed on DEC and ODEC. Mr. Andrew recommended that the Commission should impose conditions to the merger if the Commission approves it. The recommended conditions included Delmarva filing a study and implementation plan to establish procedures to reduce transmission congestion, and that the Commission monitor transmission congestion by requiring Delmarva to file reports to ensure congestion is properly managed.

27. DEC/ODEC's second witness, H. Charles Liebold, a principal with the consulting firm GDS Associates, Inc., discussed the power delivery system on the Delmarva Peninsula and its transmission congestion. Ex. 6. Mr. Liebold criticized Delmarva for inadequate planning to address the congestion and competition problems he described. These problems, he stated, increased ODEC's costs from $16,745 for the period April 1998 through June 1999 to $10,541,707 for the period July 1999 through September 2000, and that ODEC has paid $19.3 million in congestion charges for the period April 1998 through August 2001. Consequently, he recommended that the Commission should condition the merger on Delmarva's 'substantive commitments to reduce the Delmarva Peninsula transmission congestion and support a planning process that will identify projects that expand trading opportunities, better integrate the grid, and alleviate congestion.' Ex. 6 at 3. He further recommended that the Commission approve the merger only after an effective plan to reduce congestion is developed with the assistance from DEC, ODEC and Staff. Ex. 6 at 18.

28. DEC/ODEC's third witness, John Rainey, ODEC's Manager of Rates and Regulation,[5] testified about the fragility of the existing Delmarva transmission system, and how the PJM congestion model adversely impacts DEC's customers and other suppliers in the lower Delmarva Peninsula. Ex. 7. He testified that the problem arose after April 1998, when PJM began to use a Locational Marginal Pricing ('LMP') model to determine congestion pricing, and that the use of this model particularly harmed DEC beginning in July 1999 when Delmarva included transmission facilities in the PJM model and their transmission flows became subject to its LMP. As a result, he stated that ODEC and DEC have experienced excessive and volatile congestion prices, and that these costs have been passed on to their customers. Mr. Rainey testified that if Delmarva's management of its transmission system is allowed to continue unchecked, then the

resulting excessive congestion charges will ensure that no effective competitive market will develop at the wholesale or retail level because potential competitive suppliers will be unwilling to expose themselves to the congestion's price risk.

29. DEC/ODEC also presented the direct testimony of Ricardo Austria, Director of Consulting Services at Power Technologies, who sponsored studies of the Delmarva Peninsula's reliability and congestion problems and recommended improvements. Ex. 8. Mr. Austria testified that Delmarva's Peninsula transmission facilities lack the redundancy that is present in much of the remaining PJM transmission system. He concluded that high LMPs were the result of the constrained transmission system, and he noted that while Delmarva has completed and planned a series of transmission system upgrades to meet reliability criteria, these projects might not reduce congestion.

30. Mr. Rainey also presented oral testimony in support of the Proposed Settlement.

E. AES

31. AES presented prepared direct testimony of Edward Toppi, its Vice President, who testified to the possible negative effects the proposed merger would have on competing electric suppliers such as AES. Ex. 9. First, he stated that the merger would distract Delmarva from curing some of the deficiencies in its data and tariff that hinder competition. Second, he commented on Delmarva's resistance to competition and cited the peak management contracts with large customers as an example. He recommended that a customer selecting a new electric supplier should not lose their load management compensation as a result of the change in supplier. He also criticized Delmarva's slow response to AES' requests for data and the fees charged for the data.

32. In his supplemental direct testimony Mr. Toppi testified on the problems he had with the Proposed Settlement. Ex. 16. He objected to the use of frozen rates that he claimed extended the transition period until May 2006. He also objected to the frozen rates as not adequately supported, and the selection of Delmarva as the provider of SOS after the transition period. He recommended that a separate proceeding be used for the post-transition period service and rates, including a bidding process under Section 1010 of the Restructuring Act. He also opposed the Proposed Settlement's provision that would require a large customer who returns to Delmarva from a competing supplier to receive only the fluctuating MPSS' rate or a negotiated rate, as opposed to the fixed SOS rate. Finally, he recommended further efforts to promote reduced transmission congestion through establishing a working group.

F. Public Comments

33. There were five public comment sessions held and approximately twelve persons provided oral comments, which expressed concerns ranging from whether Delmarva will continue to support the local community to questions on their retirement plans.

G. Proposed Settlement

34. The record contains the Proposed Settlement, and a copy is appended to this report. Ex. 14. The Proposed Settlement is offered as a compromise to the litigation positions the settling parties presented in their pre-filed testimony, with the settling parties (except the Applicants) agreeing to withdraw their opposition to the Applicants' merger, based upon the following agreement, as summarized below: [6]

a) On October 1, 2002, Delmarva would shift the Competitive Transition Charge ('CTC') rates charged to non-residential customers from the delivery component to the supply component;

b) From October 1, 2002 through September 30, 2003, Delmarva would shift the nuclear decommissioning costs charged non-residential customers from the delivery component to the supply component;

c) From October 1, 2002 through September 30, 2003, Delmarva would amend the 'returning customer' rule set forth in its tariff so that a non-residential customer who returns to Standard Offer Service ('SOS') will pay either the Market Priced Supply Service ('MPSS') rates or a negotiated market price.

d) From October 1, 2003 through May 1, 2006, Delmarva would increase the supply components of rates charged non-residential customers to 103% of the prior rates, less the decommissioning costs;

e) From October 1, 2003 through May 1, 2006, Delmarva would increase the delivery component of rates charged residential and non-residential rates by 3%, and reduce the rates to reflect the removal of decommissioning costs;

f) Delmarva would freeze its rates effective on October 1, 2003 through May 1, 2006, except to allow Delmarva (1) to seek the recovery of extraordinary costs under 26 *Del. C.* § 1006, (2) to seek the one-time recovery once in its transmission component of rates the cost of FERC approved rate changes; (3) to seek the one-time recovery of changes in ancillary charges billed by PJM; (4) to seek to change certain optional services; (5) to seek to change its rate design if such change is revenue neutral to Delmarva and among its customer classes; (6) to seek to change its rules and regulations; (7) to seek to change the credits for load management programs; or (8) to seek to change the MPSS rate to more accurately reflect market costs;

g) Delmarva would become, pursuant to 26 *Del. C.* §§ 1006(a)(2) and 1010(a)(2), the Standard Offer Service supplier on May 1, 2003 through May 1, 2006, and to charge the Proposed Settlement's applicable rates for SOS's supply service as representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin;

h) Delmarva and BOC would terminate with prejudice the litigation in Docket No.00-653 and to enter into a special interim contract,

i) Delmarva would agree with its two existing Rate Q customers on a process to move them to different contracts and to terminate Rate Q on or before November 2, 2002;

j) Applicants would maintain the operational headquarters and significant senior management of Conectiv Power Delivery in Delaware for the next five years;

k) Applicants would maintain for the next six years its charitable contributions at levels comparable to its historic levels;

l) Applicants would make a $750,000 contribution to Murex Investments in a form that will trigger a matching federal or state funds, to the extent that such funds are available, and conditioned upon spending the funds on job training and small business development within Delmarva's Delaware service territory;

m) Delmarva would not seek recovery in rates of the merger transaction costs or the merger acquisition premium, including the merger costs if the merger does not occur;

n) Delmarva would make a $200,000 contribution to an organization designated by Staff and DPA for the promotion of renewable resources in Delaware, and to assist in informing customers of such organization;

o) Delmarva would participate in a working group to identify and develop cost effective demand side management or conservation programs;

p) Delmarva would implement a small pilot program for residential or small commercial customers to test real-time metering or similar technologies;

q) Delmarva would adopt the 'appointments kept,' 'new residential customer installations,' 'bill accuracy,' and 'outage restorations' Service Level Guarantees ('SLG') that Applicants originally had proposed, except for certain modifications, and that Applicants' remaining five proposed SLG would be addressed in separate proceedings;

r) Delmarva would modify tariff provisions to benefit competitive electric suppliers;

s) Delmarva would undertake its best efforts to develop and implement within 9 months after the merger a 'web based mechanism' to transfer its customers' historic interval data to competitive suppliers;

t) Delmarva would maintain its current construction plans for transmission facilities, except that three projects to be completed by May 2008 would be added, and that one project in the current plan would be accelerated for completion by May 2006;

u) Delmarva would implement a methodology designed to lower the congestion over its transmission system through using analysis of 'off-cost operations' data available from PJM;

v) Pursuant to 26 *Del. C.* § 1006(a)(2) d, Delmarva would file on or before March 30, 2002 schedules demonstrating its overall return based upon cost of service data;

w) Delmarva would file on or before September 1, 2005 a class cost of service study to permit a review and determination of the justness and reasonableness of its regulated rates on or after May 1, 2006; and

x) Each settling party would have the right to petition the Commission to re-open the record within 30 days of the filing of a Maryland settlement in Applicants' merger filing in that state.

35. As noted earlier, Staff witness Dillard, DPA witness Crane, Applicants witnesses Wathen and Elliott, and DEC/ODEC witness Rainey all testified in support of the Proposed Settlement, and CEPA and IBEW supported the Proposed Settlement in their written comments, and AES opposed it through testimony and the Mid-Atlantic Power Supply Association ('MAPSA') opposed it in written comments.

IV. DISCUSSION

A. Applicable Legal Standards

36. The Commission is to review the proposed merger pursuant to Sections 215 and 1016 of the Act. Section 215's pertinent part provides that:

(d) The Commission shall approve any such proposed merger, ... or acquisition *when it finds that the same is to be made in accordance with law, for a proper purpose and is consistent with the public interest.* The Commission may make such investigation and hold such hearings in the matter as it deems necessary, and thereafter *may grant any application under this section in whole or in part and with such modification and upon such terms and conditions as it deems necessary or appropriate.*

26 *Del. C.* § 215(d) (Emphasis added.).

37. The above statutory language allows the Commission considerable discretion in determining whether a proposed merger is consistent with the public interest. In addition, the Commission has broad authority to impose conditions, as it deems necessary or appropriate.

38. Section 1016(a) was added to the Public Utilities Act of 1974 as part of the amendments in the Electric Utility Restructuring Act of 1999 ('Restructuring Act'), and it provides in pertinent part that:

In approving any proposed merger, ...or acquisition, the Commission shall, in addition to considering the factors set forth in § 215 of Title 26, take such steps or condition any transfer in such a manner as to insure that any successor will continue safe and reliable transmission and distribution services.

26 *Del C.* § 1016(a).

39. This statutory language clearly intends that the Commission is to pay particular attention to the merger's impact on transmission and distribution system reliability. In addition, Section 1016(b) provides an additional set of requirements concerning a proposed merger's impact on organized labor.

40. The parties supporting the Proposed Settlement cite Section 215 where the Commission is directed to encourage settlements. 26 *Del. C.* § 215. The Applicants also cite Delaware cases where the courts discuss their review and approval of settlements. The Commission, unlike the courts, is delegated specific legislative authority to employ its expertise to protect the public interest. Nevertheless, the statute clearly requires the Commission to encourage settlements, but that does not mean blindly adopting them if they are not consistent with the public interest, the applicable law, or adequately supported by credible evidence.

41. Applicants have the burden of proof to support the Application, as amended by the Proposed Settlement. This case is presented as a contested settlement, and the only litigation is whether the Proposed Settlement should be approved, rejected or modified. Under the terms of the Proposed Settlement; however, any modification will result in the termination of the Proposed Settlement, and the settling parties would be able to pursue their respective litigation positions without prejudice to the positions that they had adopted in the Proposed Settlement.

B. Opposition to the Proposed Settlement

1. *Introduction*

42. As noted by every settling party who filed a brief, AES is the only party to oppose the Proposed Settlement. Its opposition was based upon the supplemental direct testimony of Mr. Toppi, the cross-examination of the other parties' witnesses Crane, Dillard, Wathen, Elliot and Rainey, and the legal arguments presented in the post-hearing briefs. AES' post-hearing brief presented four reasons for the Commission to reject the Proposed Settlement. The first reason is that the Proposed Settlement, if approved, would violate the Restructuring Act's provisions defining the transition period and describing the post-transition period rates for SOS. AES' second ground is that the Proposed Settlement would change the Commission's existing 'returning customer' rule in violation of the Restructuring Act and the Administrative Procedures Act and would result in a new rule that would harm competition. The third objection is that the Proposed Settlement would improperly install Delmarva as the SOS supplier after the transition period without following the selection process required by the Restructuring Act. The final reason AES advocates for rejecting the Proposed Settlement is that it would not adequately address transmission line congestion and its resulting costs, which AES submits are caused largely by DP&L's poor stewardship of its transmission system. Each of these reasons will be reviewed along with the responses in the briefs from the other parties.

2. *The Transition Period and Post-Transition Period Rates*

43. AES challenges the Proposed Settlement's provision that would establish a rate freeze beginning when the current rate freeze ends. AES views this provision as an unlawful extension of the rate freezes established during the transition period in Section 1004 of the Restructuring Act. AES IB at 2. Section 1004 states that the transition period 'shall begin on October 1, 1999 and shall end on September 30, 2002 for non-residential customers and

shall begin on October 1, 1999, and end on September 30, 2003, for residential customers.' 26 *Del C.* § 1004(a). AES further cites the statute's definitions in Section 1001(17), where 'Transition Period' is defined as 'the period of time beginning with the implementation of retail competition and ending on the dates specified in § 1004 of this title.' AES IB at 2. AES argues that the Proposed Settlement would extend this transition period until May 1, 2006 when the Proposed Settlement's rate freeze provisions would expire. AES submits that the length of time for the transition period is clearly and consistently described in the Act, and would be altered by the Proposed Settlement. *Id.*

44. In response to AES' position, Applicants, Staff, and DPA argue that the Proposed Settlement complies with the Restructuring Act. Staff states, 'nothing in the Settlement suggests extending the transition period beyond those dates provided in Section 1004 of the Act.' Staff RB at 5. Delmarva points out that the Proposed 'Settlement does not extend the statutory Transition Periods.' DP&L RB at 7. DPA also notes that the Proposed Settlement does not alter the transition period, but in fact recognizes the end of the statutory transition period because the Proposed Settlement's proposed rates are to go into effect after the transition period. DPA RB at 2.

45. The arguments in opposition to AES' position may be brief, but their brevity is based upon their inherent and obvious correctness. AES is correct that the Restructuring Act defines the transition period and when it ends. The other parties also rely on the statute for their opposition, which is based on the fact that nothing in the Proposed Settlement changes the statutory transition period or possibly could change it. AES attempts to focus on the Proposed Settlement's rate freeze provision as being similar to the rate freeze during the transition period, but the fact remains that the Proposed Settlement's rates will go into effect after the transition period and be higher than the transition period's rates. The mere fact that a rate freeze will be in place, albeit at higher rates, cannot be construed as extending the transition period, which is not changed by the Proposed Settlement and could only be changed by an amendment to the statute.

46. AES also argues that the Proposed Settlement would violate the Restructuring Act's ratemaking directives because it would establish rates contrary to Section 1006(a)(2), which states that the rates in effect after the transition period 'shall be representative of the regional wholesale electricity market price, plus a reasonable allowance for retail margin to be determined by the Commission if DP&L is a Standard Offer Service ('SOS ') supplier.' AES witness Toppi testified that there is nothing in this proceeding supporting that the rates proposed in the Proposed Settlement are representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin as required by the Restructuring Act. Ex. 14 at 2-3. AES argues that Applicants witness Wathen's testimony is insufficient since he summarily concluded that the 'proposed rates coming out of the settlement are reasonable.' AES IB at 3, Tr. 245. AES submits that it is not possible for the Commission to determine whether the rates in the Proposed Settlement meet the criteria under Section 1006(a)(1)(a) without evidence on how they were derived. Instead, AES concludes, the Commission must review evidence of the representative wholesale regional electric market price and a reasonable allowance for the retail margin. AES also finds 'even more disturbing is the fact that the rates proposed under the Settlement, are based upon the current rates, which were also determined in the course of Settlement negotiations and may or may not reflect actual cost.' AES IB at 3. AES then poses the rhetorical question, namely, 'that although Witness Crane and other parties believe the Proposed Settlement is a good deal for ratepayers, how could anyone know if it is or is not a good Deal?' AES IB at 3. In effect, AES questions the quality of the record and whether it contains sufficient evidence to support the Proposed Settlement as consistent with the Restructuring Act.

47. Delmarva answers this question by citing the testimony of the witnesses who testified in support of the Proposed Settlement's rates. DP&L RB at 6. This testimony, Delmarva submits, provides the Commission with an adequate record and evidentiary support for the Proposed Settlement. *Id.* Delmarva asserts that the Proposed Settlement is reasonable, in the public interest, and adequately supports designating Delmarva as the default service provider and charging the rates developed in the settlement process. DP&L RB at 9-12.

48. DPA also refutes the AES criticism by citing to the testimony of witnesses Wathen and Dillard, which DPA states provide support for the Commission's determination that the end result is reasonable. DPA RB at 4. DPA also points out that the Commission in Delmarva's restructuring proceeding reviewed the end result of a settlement

to establish just and reasonable rates during the transition period, which were to be based on the same standard, namely, representative of the regional wholesale electric market price plus a reasonable allowance for retail margin.

49. Staff addressed this issue and also noted the identical statutory language is used for the transition period rates and the post-transition period rates, namely, 'regional wholesale electric market price, plus a reasonable allowance for retail margin.' Staff emphasizes that the Commission accepted the current transition period rates based upon a contested settlement, and that it should again approve a settlement in this case although it may be contested. Staff RB at 7.

50. Based upon the parties' arguments and the record, the Proposed Settlement does not violate Section 1006. The Proposed Settlement states the parties agreement that the post-transition rates, as described in the Proposed Settlement, comply with Section 1006's requirement for a 'regional wholesale electric market price plus a reasonable allowance for retail margin.' Ex. 14 at 10, ps D.1. Thus, the Proposed Settlement's language clearly is based upon Section 1006, and the Commission will make the necessary determinations required by Section 1006 if it approves the Proposed Settlement.

51. AES still questions whether adequate evidence supports the Proposed Settlement's rate provisions. The Proposed Settlement's provisions on the post transition period's rates are supported by substantial evidence in the form of the opinion testimony of three expert witnesses. Staff witness Dillard, Applicants witness Wathen, and DPA witness Crane concluded that the Proposed Settlement's rate provisions are reasonable and should be approved as consistent with Section 1006. These witnesses provide sufficient supporting testimony that the Commission may reasonably rely upon in determining that the Proposed Settlement's rates are representative of the regional wholesale market electric price, plus a reasonable allowance for retail margin. Therefore, the Proposed Settlement's rates are supported and would comply with Section 1006.

52. Section 1006 did not change the Commission's authority to approve rate settlements when they are adequately supported and in the public interest. Section 1006 requires only that this Commission make a finding that the rates are 'representative of regional wholesale electric market prices, plus a reasonable allowance for retail margin.' The Restructuring Act does not dictate to the Commission how to make that finding. If the Commission determines, based upon the record evidence of the witnesses, that the Proposed Settlement's end result is reasonable and representative of the region wholesale electric market price plus a reasonable allowance for retail margin, then Section 1006 is satisfied. I agree with Applicants' argument that adequate support for a settlement does not require the same evidence as a fully litigated case. AES would have this Commission require the parties to produce the specific ratemaking ingredients that went into the Proposed Settlement. No settlement could be supported if the parties' had to agree on the 'correct' ratemaking recipe used to support the end result. Instead, the settling parties agreed on rates that are an end result consistent with Section 1006. AES' criticism, if accepted, would eliminate one of the benefits of any settlement, namely, a quicker and less costly resolution of litigation. I also agree with Staff's argument that the Commission already approved the transition period rates under the same standard as Section 1006, and this approval was based upon a settlement that was more contested than the Proposed Settlement.

53. AES' point that the Proposed Settlement's supporting evidence is less than the support in a rate case also means that AES could easily have rebutted the evidence with its own evidence. Instead, AES relied only on the argument that the Proposed Settlement lacked support. AES had the opportunity to present its own evidence showing that the Proposed Settlement's rates are not 'representative of the regional wholesale electric market price, with a reasonable allowance for retail margin.' AES did not and seeks to defer any post-transition ratemaking to another proceeding. The issue properly has been included in this proceeding, and the ratemaking issues need not be deferred. It is reasonable and consistent with the Commission's authority over mergers to impose ratemaking conditions. The rate conditions in the Proposed Settlement are reasonable and adequately supported. Under the Proposed Settlement, the post-transition rates will be slightly higher than the present rates that this Commission already approved based upon a decrease in the monopoly distribution rates and an increase in the competitive supply rates. The overall changes are less than 1% increase. Moreover, the rates will remain in effect from the end of the transition periods until May 2006, which is a significant benefit to ratepayers. The Commission in a fully litigated rate case would not have any power to order

Delmarva to freeze its rates. Thus, the Commission's authority to approve a merger properly should consider the Proposed Settlement's rates as an overall benefit consistent with the public interest and Section 1006 of the Restructuring Act.

54. AES also belatedly complains about the proceeding's lack of time to investigate the Proposed Settlement's rates, and states 'the procedural schedule established in this case did not permit additional discovery after the filing of the Settlement to allow the parties to even attempt to ascertain the appropriateness of the proposed rate changes.' AES IB at 7. AES may have had a valid complaint if it had been raised when the procedural schedule was being revised to consider the Proposed Settlement. AES waited until the briefing stage to voice its objection. Following the November 18, 2001 hearing, the parties proposed a consensus revised procedural schedule, which I approved. AES either concurred in the procedural schedule or did not voice any objection at the time. Consequently, its argument that there was insufficient time to investigate the Proposed Settlement's rates is rejected as either untimely or waived. A party who raises procedural problems needs to do so when such problems may be corrected or else suffer the consequences of having its silence deemed consent to the procedures. Thus, under the circumstances presented in this case, [7] the Proposed Settlement should not be rejected on the ground that AES did not have an adequate opportunity to develop the record in opposing the Proposed Settlement because AES had the opportunity and did present its position through supplemental direct testimony.

3. *Change to the 'Returning Customer' Rule*

55. AES objects to the Proposed Settlement's provision that would change, effective October 1, 2002, the current tariff's rule that controls the rate options available to a large customer who returns to Delmarva's supply service from a competing supplier. AES IB at 9-14. The Commission established the current rule when it approved Delmarva's restructuring plan and implementing tariff in Docket 99-163. The current rule allows a 'returning customer' to select either Delmarva's fixed transition period rates with a twelve month service commitment or its monthly changing Market Pricing Standard Service ('MPSS') without any twelve month commitment. The Proposed Settlement would eliminate the fixed rate option for SOS in the post-transition period.

56. AES argues that the Proposed Settlement's change would discourage competition by providing customers who do not leave Delmarva with an unfair advantage of receiving the fixed rate option over customers who switch suppliers. *Id.* at 9. AES also contends that the change is contrary to Section 1006's mandate that Delmarva must offer SOS to every 'returning customer.' The pertinent part of Section 1006 is set forth below:

Standard Offer Service price shall be the applicable retail market price for Electricity Supply Service for any Customers who have not chosen an alternate Electric Supplier or have returned to obtaining their Electric Supply Service for the Standard Office Service Supplier, subject to such regulations as the Commission may adopt pursuant to § 1010(c) of this title for returning customers.

26 *Del. C.* § 1006(a)(2)(ii).

57. AES further cites that Section 1010(c), which states that 'the Commission shall promulgate rules and regulations governing ...customers who leave the standard office service supplier and later return to the standard office service provider.' AES IB at 9. This citation, AES contends, supports its argument that the Commission must conduct a rulemaking before any change to the 'returning customer' rule. Finally, AES submits that the Commission has not followed the Administrative Procedures Act ('APA'), 29 *Del. C.* § 10101 *et seq.*.' AES IB at 10. Specifically, AES submits that Section 10102(7) defines a rule as 'any statement of law, procedure, policy, right, requirement or prohibition formulated and promulgated by an agency as a rule or standard, or as a guide for the decision of cases thereafter by it or by any other agency, authority or court.' and that the change in the Proposed Settlement would be a changed rule under the APA. 29 *Del. C.* § 10102(7).

58. Applicants' response to AES' argument is first to dispute that any Commission regulation would be amended. DP&L RB at 20-23. Applicants further dispute that the Proposed Settlement's 'returning customer' provision would

violate Section 1006 in allowing the customer to only receive MPSS or a negotiated rate. Applicants cite Section 1010(c), which they contend specifically allows the Commission to establish market pricing for returning customers. DP&L RB at 23. Finally, Applicants contend that the Proposed Settlement's 'returning customer' provisions will encourage competition and point to the support by the parties that will be affected by the change. DP&L RB at 24-28.

59. Staff also addressed this issue and stated that AES has confused the Delmarva restructuring proceeding with the Commission's rulemaking proceeding in Regulation Docket No. 49. Staff RB at 10-12. The current provision, Staff states, was established in the restructuring proceeding and not in a rulemaking proceeding. Staff also notes DEUG's support of the Proposed Settlement even though its members will be affected by the change. Staff RB at 12. Finally, Staff dismisses AES' argument of undue discrimination as without merit because the Commission can set different rates for different customers with different usage when such usage causes different costs to be incurred. Staff RB at 12.

60. DPA supports the Proposed Settlement's change and notes that the Proposed Settlement would not alter any rule or regulation, but instead would change Delmarva's tariff. DPA RB at 6-7. DPA points out an inconsistency in AES' position when it argues against using market based rates in the Proposed Settlement's 'returning customer' provision while opposing the Proposed Settlement's SOS rates as not market based. DPA RB at 7.

61. The 'returning customer' rule was addressed in Delmarva's restructuring proceeding and the Commission's rulemaking proceeding. See Order No. 5206, Docket No 99-163 (August 31 1999), Order No. 5227, Docket No. 99-163 (September 28, 1999), and Order No. 5207, Regulation Docket No. 49 (August 31, 1999). The concern in these proceedings was that a 'returning customer' could abuse or 'game' the system by selecting the fixed rate during the high cost periods, such as the summer peak months, and then leave the fixed rate during the low cost periods, such as the winter off-peak months. The switching would result in Delmarva serving a 'returning customer' during high cost periods based upon rates developed from annual average costs. As Applicants note, the Restructuring Act in Section 1010(c) also allows the Commission to impose reasonable conditions on the 'returning customer's' service in order to protect Delmarva's other customers.

62. The first question AES raises is whether any change in the 'returning customer' rule must comply with the APA's rulemaking procedures in 29 *Del. C.* § 10118, which require a cumbersome and lengthy process in order to change a rule. Admittedly, the APA's rulemaking process has not been followed in this proceeding or will be followed in the future under the Proposed Settlement. The answer to AES' question is apparent from the procedure the Commission used in Docket No. 99-163, which, as Applicants point out, was a case decision procedure under the APA and not an agency rulemaking.

63. The difference between a tariff rule change and a rule established in a rulemaking may blur the line between a case decision and a rulemaking, but the Commission clearly determined in Order No 5207 that it was not addressing the rules for 'returning customers' in that rulemaking proceeding. The regulation promulgated in Regulation Docket No. 49's rules in Section IX state that '[t]he procedures for a Retail Customer's return to an EDC during the Transition Period and to a SOS Supplier after the Transition Period for Electric Supply Service shall be in accordance with the Commission's order for each EDC's individual electric restructuring plan.' The Commission's discussion of the above-quoted rule, refers the issue to its case decision on this issue in Delmarva's restructuring plan, as set forth below:

That section IX of the Commission Staff's proposed rules is not adopted. Instead, the Commission orders that the retention issues be handled as part of the individual utility's restructuring plan.

Order No. 5207 at Ordering

64. Applicants, Staff and DPA are correct that the Proposed Settlement would not amend any rule or regulation. Instead, only Delmarva's tariff would change. I also agree with AES that this proceeding cannot change a regulation because it is not a rulemaking proceeding. In the above-quoted Order, the Commission already addressed AES's issue and ruled against promulgating any regulations for 'returning customers.' While the regulation refers to Delmarva's restructuring plan and not to a merger application, I find that the Proposed Settlement will amend the tariff that the

Commission approved in the restructuring proceeding and, consequently, the Commission may reasonably consider this tariff change to be part of Delmarva's restructuring plan and consistent with the rule in Regulation Docket No. 49.

65. AES' argument that a 'returning customer' is entitled to SOS under Section 1006 has some merit. Under the Proposed Settlement, MPSS or a negotiated contract would be the only two options available for a 'returning customer.' I agree with Staff that the Commission can determine different rates for different customers based upon their different usage. Indeed, the transition period rates are different for each rate class. This ratemaking discretion to discriminate, albeit not unduly, between customers also supports the Proposed Settlement's 'returning customer' tariff change. The effect of the Proposed Settlement will not deny SOS to a 'returning customer.' Instead, it will provide the 'returning customer' with SOS in the form of the MPSS tariff or a negotiated contract. The Restructuring Act defines SOS as 'the provision of electric supply service after the transition period by a standard offer service suppliers to customers who do not otherwise receive electric supply service from an electric supplier.' 26 *Del. C.* § 1001. Under this definition, a 'returning customer' is entitled to SOS, but there is nothing that mandates that a returning customer receive the same SOS as other customers.

66. There also is nothing in the Restructuring Act that requires fixed SOS rates, only that they be 'representative of regional wholesale electric market price, plus a reasonable allowance for retail margin.' In theory, a market price is not fixed. Consequently, it is reasonable for the Commission to determine that the flexible rate in MPSS is appropriate as the SOS for Delmarva's larger customers. The use of flexible rates for some customers and fixed rates for other customers is supported by the Commission's approval of flexible rates for certain customers who are particularly responsive to market energy prices. Consequently, the use of MPSS' flexible pricing for SOS does not constitute undue discrimination, but is based upon the same concerns that the Commission addressed in the restructuring proceeding.

67. In Delmarva's restructuring proceeding, the Commission recognized that returning customers could impose higher costs and respond to market conditions and competition more than other customers. *See* Order No. 5231 at 33-34. Consequently, the Commission required a twelve month retention period for Delmarva's large 'returning customers' based upon Section 1010(c) of the Restructuring Act, as set forth below:

*5 The Commission shall promulgate rules and regulations governing the amount of notice that a Customer who desires to return to the Standard Offer Service Supplier must provide, the minimum amount of time that a Customer must take service from a Standard Offer Service Supplier, and the amount of charges that may be assessed against a Customer who leaves the Standard Offer Service Supplier and later returns to the Standard Offer Service Supplier, *including the appropriate retail market price, which may be higher than the Standard Offer Service Price.*

26 Del C. § 1010Cc) (emphasis added).

68. The above language clearly allows the Commission to establish for 'returning customer' 'appropriate retail market price' rates 'which may be higher than the Standard Offer Service Price' available to other customers. This statutory authority is consistent with the Proposed Settlement's use of MPSS as the SOS for a 'returning customer.' I find that the MPSS or negotiated contracts options are appropriate for returning customers as their SOS in order to protect Delmarva and its other ratepayers from the adverse consequences of gaming by large customers, who are particularly responsive to changes in market prices for their electricity.

69. Thus, the Proposed Settlement's modification to the 'returning customer' rule in Delmarva's tariff is reasonable, does not require the Commission to institute a rulemaking proceeding, and is consistent with Sections 1006 and 1010 of the Restructuring Act and the public interest in protecting Delmarva's customers and shareholders from the adverse consequences of economic decisions made by Delmarva's largest customers. [8]

4. Establishing Delmarva as the Standard Offer Service Supplier

70. AES's third issue with the Proposed Settlement is that it improperly establishes Delmarva as the SOS supplier following the transition period and continuing until May 1, 2006. AES IB at 14-17. AES' argument relies on the procedure whereby the Application for a merger included selecting Delmarva as the SOS supplier. Similar to its argument on the 'returning customer' provision, AES contends that the Proposed Settlement would violate the APA and the Restructuring Act.

71. Applicants respond to AES' argument by disputing that the APA's rulemaking provisions control. DP&L RB at 13. Instead, Applicants state that the APA's provisions on case decisions govern the Commission's consideration of the Application and that there is an adequate record to support the Proposed Settlement as a case decision under 29 Del C. §§ 10121-28. Applicants set forth the evidence that supports Delmarva as the SOS provider, including the 'price, reliability and overall quality of the electric supply service offered under 26 *Del. C.* § 1010(a) (2). DP&L RB at 14-15. The Applicants also object to AES' attempt to refer to matters outside the record in AES' Initial Brief. DP&L RB at 15-16.

72. Staff argues that AES's opposition to Delmarva's selection as the SOS provider should be rejected because there was adequate notice of this issue, the end result under a bidding scenario may have produced higher rates than the Proposed Settlement's, and that there was an adequate inquiry into the reasonableness of the end result. Staff RB at 12-15. DPA also supports Delmarva as the SOS provider because adequate public notice occurred and AES admitted that it was unable to generate interest in the proceeding through its own efforts. DPA RB at 7-8.

73. The Proposed Settlement's provision that Delmarva would be the SOS provider was not in the Application, but was raised in the course of the litigation of the Application. Consequently, AES is correct that the Commission's original public notice did not refer to this issue. In order to provide public notice, a second public notice of the terms of the Proposed Settlement was published in the same form as the original notice, and prompted a response by Mid-Atlantic Power Supply Association ('MAPSA'). AES cites MAPSA's response to support its position that inadequate notice occurred. Contrary to AES' position, the fact that MAPSA filed comments in response to the notice demonstrates that adequate public notice of the Proposed Settlement occurred.

74. Many cases begin with what the utility seeks, which is the subject of the initial public notice. Thereafter the case may change as other issues are added by the opposing parties' different litigation positions. The public notice of the Application placed interested persons on notice that the Commission proceeding on the Application had commenced, and that is all that the law requires. The notice is intended to inform an interested person of the right to petition to intervene. The wide range of parties who intervened attests to the success of the Commission's initial public notice to attract interested parties. The supplemental public notice that was published in this case recognized that the Proposed Settlement expanded the scope of the proceeding from a mere merger approval. This notice again provided interested persons with an opportunity to be heard on the Proposed Settlement and its rate provisions. Consequently, given these opportunities to be heard, the Proposed Settlement and the Commission's approval of it will not violate due process, particularly AES' rights since it was a party throughout the proceeding.

5. *Transmission Line Congestion*

75. The final issue AES raises in opposition to the Proposed Settlement is that the Proposed Settlement does not provide adequate relief to competitive energy suppliers for escalating congestion costs caused largely by DP&L's poor stewardship of its transmission system. AES IB at 19-22. Accordingly, AES urges the Commission to establish a working group to provide a more effective mechanism for holding DP&L accountable for the excessive congestion in its service territory. AES Brief at 21. In support of its position, AES refers to the testimony of DEC/ODEC witnesses Austria and Rainey.

76. Applicants argue that the Proposed Settlement adequately addresses the transmission congestion issue that was raised by the pre-filed testimony of DEC/ODEC and Staff witnesses. DP&L RB at 28-33. Applicants set forth five arguments that support the Proposed Settlement and reject AES' opposition. Staff also argues that the Proposed Settlement adequately addresses the transmission congestion issue, and highlights that the settlement pro- cess

constituted a 'working group' that AES attempts to have the Commission establish. Staff RB at 15. Staff points out that the Proposed Settlement will reduce transmission congestion, which will benefit all suppliers. Staff RB at 17.

77. DPA supports the Proposed Settlement's provisions that are designed to reduce transmission congestion, which DPA submits should be allowed to work before the Commission considers other measures such as the working group that AES has proposed. DPA RB at 8-9. DEC/ODEC also argue that the Proposed Settlement is adequate and responsive to its interests as well as other suppliers. DEC/ODEC RB at 2-6. DEC/ODEC, as a proponent of changes to Delmarva's operation of its transmission system, recognizes that the Proposed settlement is a compromise, but it is one that they support because it would establish a process to reduce transmission congestion. DEUG and BOC, as representatives of large customers, also support the Proposed Settlement's transmission congestion provisions.

78. DEC/ODEC, BOC and DEUG also argue in support of the Proposed Settlement's transmission provisions. The support of these parties is particularly comforting in light of DEC/ODEC's strong testimony in opposition to Delmarva's operation of its transmission system.

79. The Proposed Settlement's provisions are complex and attest to the settling parties' time and effort in fashioning an acceptable mechanism to address the transmission congestion issue raised in this proceeding by DEC/ODEC and Staff witness Glover and Dillard. AES' criticism of the Proposed Settlement is that it does not require a working group. As Staff notes, the settlement process itself was a working group. Thus, I find that AES's criticism is nothing more than nitpicking. The record is uncontested that the Proposed Settlement's provisions on transmission congestion will benefit AES, other suppliers, and the customers of DEC and Delmarva. I agree with DPA that the Proposed Settlement's mechanism should be allowed to work before the Commission intervenes and imposes additional steps, even as benign as establishing a working group. The Commission has an open rulemaking proceeding on reliability where the transmission issues may be pursued further, either formally or informally. In sum, the Proposed Settlement provides an acceptable compromise mechanism to address the difficult and complex problem of transmission congestion, and should be approved and allowed to work before any changes are considered.

*6 *C. The Proposed Settlement And Applicable Legal Standards*

80. The above discussion of AES' objections to the Proposed Settlement does not address the ultimate issue for the Commission to decide, namely, whether the Proposed Settlement, taken as a whole, satisfies Section 215's standard that the proposed merger is in accordance with law, for a proper purpose and is consistent with the public interest, as well as Section 1016's standard that any successor will continue to provide safe and reliable transmission and distribution services. Applicants set forth in their brief the reasons that the Proposed Settlement was consistent with the applicable law because of the benefits for ratepayers, competitors, the community, and the transmission and distribution system. Staff, DPA, DEUG, DEC/ODEC, and BOC also argue that the Proposed Settlement was consistent with the applicable legal standards.

1. ***Ratepayer Benefits***

81. DPA, as the primary representative of ratepayers, presented Ms. Crane to explain why DPA supported the Proposed Settlement. First, she stated it would benefit ratepayers because of the freeze of distribution, transmission and ancillary service rates from the end of the transition period until May 1, 2006, with some exceptions. Tr. 291-92. Second, she said it would adopt customer service level guarantees. *Id.* Third, she testified that the Proposed Settlement would eliminate any risk that ratepayers might be asked to pay for merger related costs, thereby ensuring that ratepayers would not be charged with the expenses of the merger. *Id.* Fourth, Ms. Crane noted the benefits to larger customers in the form of settling issues involving BOC and Rate Q customers. Tr. 292-93. Fifth, she expressed support for the Proposed Settlement's commitments to enhance reliability and to reduce transmission congestion. Tr. 295.

82. Staff presented Ms. Dillard to testify in support of the Proposed Settlement and she identified as a benefit the Proposed Settlement's provisions that strengthened some of the Applicants' original customer service guarantees. Tr. 309. Ms. Dillard further noted the Proposed Settlement's benefit whereby Delmarva agrees to forego recovery of various merger-related costs. She also addressed the benefit in Delmarva's participation in a working group that will identify cost effective demand side management conservation programs; and that the Applicants have agreed to participate with Staff in a pilot program for advanced metering. Tr. 309-10.

83. Applicants' witness Wathen also testified that the Proposed Settlement was beneficial to ratepayers because of its proposed increase in overall rates that were generally below 1% — ranging from an increase of about 0.3% to an increase of 1.4% and these levels would then be frozen until May 2006 with some exceptions. Tr. 234-36, 242-43; Ex. 14 at 3-11; see also Ex. 19. He explained that for a very modest rate change averaging less than 1% as of October 2003, ratepayers will enjoy a price freeze for nearly three years beyond the currently effective rate freeze, and that the Proposed Settlement calls for a decrease in the regulated distribution component of rates. Tr. 234, Tr. 245. He testified that the Proposed Settlement's increase to the supply components of rates would promote competition and could be avoided by a customer's selection of a lower cost supplier. Tr. 245. Mr. Wathen concluded that these proposed rates were reasonable and were the product of extensive negotiations among parties that represented a wide range of interests. Tr. 245.

84. Applicants witness HasBrouck set forth Delmarva's initial service level guarantees, and the Proposed Settlement incorporates four of these proposals with minor modifications and defers five others to other dockets. These service level guarantees are essentially unmatched: 'few utilities in the U.S. have committed to a comprehensive package of guarantees that matches the Companies' proposal.' Ex. 4 at 9. DPA and Staff supported the Company's service level guarantees in concept, proposing modifications, as they deemed appropriate. Ex. 10 at 28-34; Ex. 13 at 16-21. The Proposed Settlement makes some, albeit not all, of the recommended DPA and Staff modifications, but these parties fully support the Proposed Settlement as an acceptable compromise. Tr. 292, 303, 309.

85. The Proposed Settlement's rate freeze provisions also will indirectly capture the merger-related savings, which DPA witness Crane had addressed as one of her initial concerns with the merger. Ex. 10 at 10-13. Any savings would have to overcome the portion of the $46 million in estimated merger transaction costs. Moreover, the savings also will be eroded by any inflation over the three-year period of the rate freeze. The $543,100,000 in the acquisition premium that Pepco is paying to acquire Conectiv also could not be recovered from ratepayers, although this Commission has not recognized such premiums in rates. Tr. 330. *See* Order No. 5592 at 9-12, Docket No 99-466 (November 22, 2000). Staff witness Glover also was concerned with increasing supply costs, which will be controlled by the Proposed Settlement.

2. *Competition Benefits.*

86. Applicants contend that the Proposed Settlement provisions are consistent with competition, and cite DPA witness Crane's testimony on the increase to the shopping credit and certain specific provisions that will facilitate the exchange of information with competitive suppliers. Tr. 293-95. Applicants witness Wathen similarly testified that the Proposed Settlement would increase the shopping credits between 2.7% to 8.4%, which would enhance competition. Tr. 236, Ex. 19. He said that for most customer classes, the resulting shopping credits would be higher than or in-line with the shopping credits applicable with respect to most nearby utilities. Tr. 237-38, Ex. 17.

87. Applicants note that the Proposed Settlement also promotes competition by incorporating specific recommendations that AES had sought in this proceeding. For example, AES witness Toppi testified that certain Delmarva contracting practices for peak management customers discouraged competition, and the Proposed Settlement includes changes that would satisfy this AES concern. Ex. 9 at 3-5, Tr. 178. Similarly, AES sought modifications to certain Delmarva's electronic data information exchange protocols and the provision of data to competitive suppliers, and the Proposed Settlement satisfied this concern. Ex. 9 at 8-10, Tr. 178. AES supports some of the Proposed Settlement, but the Proposed Settlement is submitted as a complete package and cannot be unbundled without destroying it. As a whole, the Proposed Settlement should benefit the competitive environment through higher shopping credits, and the changes

that AES sought. Even the elimination of the SOS option for returning customers will benefit competition because the availability of SOS service provides another reason to return to Delmarva's service from a competitor's supply service.

3. Community Benefits

88. Applicants also describe the Proposed Settlement's provision on maintaining the headquarters and a significant senior management in Delaware for a minimum of 5 years as a benefit. DPA witness Crane concurs that these are benefits. Tr. 249. In addition, the Proposed Settlement will require Delmarva to maintain its current level of charitable contributions in Delaware for a minimum of 6 years. Again, this is an important benefit for the community and one that the Commission could not have imposed on Applicants as a condition to the merger without intruding on Applicants' managerial discretion. The Proposed Settlement also requires Delmarva to invest or contribute $750,000 to a job training/economic development organization. This is consistent with Section 1016's concerns with organized labor. In addition, the Proposed Settlement will require Delmarva to spend $200,000 to promote renewable resources, which will benefit the community. Tr. 249. Mr. Wathen testified that none of these conditions in the Proposed Settlement are required under Delaware law or regulation, but are a direct benefit of the Proposed Settlement. Tr. 248-49. I agree with Mr. Wathen's assessment, although the Commission may have been able to condition its approval by including some of the commitments if supported by evidence.

89. CEPA's support of the Proposed Settlement is based on many of the same reasons as the other parties, including the funds for renewable resources and the extensions of the price freezes for SOS. Ex. 18. IBEW, as a representative of organized labor, also provides important support of the Proposed Settlement as consistent with the public interest and Section 1016's concerns with the impact of a merger on organized labor.

5. Transmission and Distribution Reliability Benefits

90. Section 1016 of the Restructuring Act added a new consideration for the Commission in its review of an electric utility's application for approval of a merger, namely, whether the successor utility will continue to provide safe and reliable transmission and distribution services. The record supports finding that the Proposed Settlement satisfies this requirement.

91. The record supports that the merger will not change Delmarva's operations, which will continue to operate as a separate utility under a new parent corporation. The Applicants' supporting testimony emphasized their commitment to reliable and safe transmission and distribution services. While the ability of Delmarva to operate its transmission system efficiently seriously was challenged by DEC/ODEC and Staff witnesses, the Proposed Settlement gained these parties support with its provisions that add three transmission projects and which accelerates dates in the current Delmarva capital plan for new transmission facilities. Ex. 11 at 6, Ex. 14 at 23, Tr. 282. The issue of transmission congestion also is included in the Proposed Settlement, which establishes a mechanism to reduce congestion and costs and this too should also improve the reliability of the transmission system to the extent that congestion may lead to failure. This mechanism establishes a threshold of congestion, which, once crossed, would trigger Delmarva to plan for reducing the congestion. The mechanism is based upon Staff witness Glover's testimony and should be approved as an interesting effort to resolve a difficult issue.

5. Conclusion

92. Based upon the record, I find that the Proposed Settlement convincingly is a comprehensive package that should be approved under the applicable legal standards. The Proposed Settlement reflects a compromise among competing interests that form a spectrum of interests. These interests, taken together, may reasonably be considered as representative of the public interest, particularly with the support of Staff and DPA. The opposition of AES, as a competing electric supplier, has been considered, but its objections do not convince me that any change is appropriate, particularly when to do so may jeopardize the provisions of the Proposed Settlement that AES supports. On balance, the Proposed Settlement, if adopted, should improve the competitive environment.

93. I agree with Applicants witness Wathen that the Proposed Settlement includes provisions that could not otherwise have been obtained through litigation. The Commission should approve the Proposed Settlement as the only way to obtain these benefits, which Applicants' have voluntarily provided as conditions in order to advance their goal of obtaining the settling parties' support for the Proposed Settlement and ultimately the Commission's approval of the merger. The Commission should approve the Proposed Settlement in order to obtain the benefits for ratepayers, shareholders, competitors, and the community.

94. The Proposed Settlement's provisions that will establish post-transition SOS rates and Delmarva as SOS provider are particularly noteworthy. These provisions will eliminate a major source of uncertainty in the future cost of electricity to Delmarva's customers. If energy prices escalate, then customers are protected under the Proposed Settlement. If energy prices fall, then customers can select a lower cost supplier than Delmarva. I find that Staff's review of the existing Delmarva supply contracts as particularly comforting in that Staff witness Dillard's independent review supports that Delmarva can provide SOS at the Proposed Settlement's rates above its costs. Tr. 312-13. Competing electric suppliers now have a target to aim at for their pricing, and their failure to compete may be more attributable to their failure to lower costs or their expected returns than to an unfair regulatory environment.

95. I also note that the Proposed Settlement does not include proposed tariffs to implement the Proposed Settlement, except for the proposed MPSS tariff. I agree that approving tariffs may be premature this far in advance of their effective dates. Furthermore, any subsequent proposed tariff filed to implement the Proposed Settlement, if approved, may provide additional opportunities to be heard. The Commission's approval of the Proposed Settlement will allow the proposed merger to go forward with one less regulatory obstacle, and will provide substantial benefits to ratepayers, competitors, and the community.

V. *RECOMMENDATIONS*

96. Based upon the record and arguments presented and the above reasoning, I submit for the Commission's consideration the following recommendations:

*7 a) That the Commission reject the objections of AES to the Proposed Settlement;

b) That the Commission approve the Proposed Settlement, attached hereto as Appendix A, in its entirety and without modification;

c) That the Commission determine that the rate provisions of the Proposed Settlement are consistent with Section 1006 of the Restructuring Act;

d) That the Commission approve the Application, as modified and conditioned by the Proposed Settlement; and

d) That the Commission reserve the right to issue such orders as may be necessary to implement the Proposed Settlement, including the approval of tariffs.

Respectfully submitted,

Robert P. Haynes Hearing Examiner

APPENDIX A-PROPOSED SETTLEMENT

PROPOSED SETTLEMENT

On this day, November 30, 2001, Delmarva Power & Light Company ('Delmarva '), Potomac Electric Power Company ('Pepco'), Conectiv Communications, Inc. ('CCI') and New RC, Inc. ('New RC') (together, the 'Applicants') and the other undersigned parties (all of whom together with the Applicants are the 'Settling Parties') hereby propose a settlement of all issues in these proceedings.

I. *BACKGROUND*

On May 11, 2001, the Applicants, including Conectiv Communications, Inc. ('CCI '), filed an application (the 'Application') before the Delaware Public Service Commission ('Commission') pursuant to 26 *Del. C.* §§ 215 and 1016 seeking permission to transfer indirect control of Delmarva and CCI to New RC and Pepco. [9] Included in support of the Application was pre-filed testimony: 1) jointly by Pepco Chairman and Chief Executive Officer John M. Derrick, Jr. and Conectiv President and Chief Operating Officer Thomas S. Shaw; 2) Dr. Joe D. Pace; and 3) Mr. Derek W. HasBrouck.

The proposed transfer of control will be effectuated through a series of transactions, as set forth in the Application and in more detail in the Agreement of Merger attached to the Application. In brief synopsis, Delmarva's corporate parent, Conectiv, will become a wholly-owned subsidiary of a new holding company, temporarily named New RC. Pepco will also be a wholly-owned subsidiary of New RC. The end-result is that New RC will own, directly, or through Conectiv, three operating utility companies, Pepco, Delmarva and Atlantic City Electric Company.

On May 22, 2001, in Order No. 5722, the Commission established this proceeding, assigned the matter to the Hearing Examiner, established a date for an initial pre-hearing and public conference of June 18, 2001, and ordered newspaper publication of a notice of the Application and Commission Order, which notice also specified a deadline and method for filing petitions to intervene. Public notice of the Application and Commission Order was duly published (Ex. 1).

*8 At the June 18, 2001 pre-hearing conference, a procedural schedule was developed and approved. Public hearings were also scheduled and held on September 10, 2001, in Wilmington, Delaware, September 12, 2001, in Dover, Delaware, and September 18, 2001, in Georgetown, Delaware. Transcripts of those public hearings were taken. In addition, evidentiary hearings were scheduled to begin on November 28, 2001.

Either as the result of timely intervention or unopposed late intervention, the parties to this case, in addition to the Applicants, Commission Staff ('Staff') and the Division of the Public Advocate ('DPA '), are: International Brotherhood of Electrical Workers ('IBEW') Local Union 1307; BOC Gases, Inc. ('BOC'); the Consumers Education & Protective Association of Delaware ('CEPA '); Mr. Bernard J. August; Cable Telecommunications Association of MD, DE &DC; Old Dominion Electric Cooperative ('ODEC'); the Delaware Electric Cooperative ('DEC'); the Delaware Energy Users Group ('DEUG '); and AES NewEnergy, Inc. ('NewEnergy').

On or about October 17, 2001, direct testimony was submitted by certain parties to this proceeding. Staff submitted testimony by Ms. Janis L. Dillard, Dr. John Stutz, and Dr. J. Duncan Glover. DPA submitted testimony by Ms. Andrea C. Crane. ODEC and DEC submitted testimony of: J. William Andrew, Ricardo R. Austria, John Rainey, and H. Charles Liebold.

In October, informal settlement meetings to which all parties were invited were also held. On November 1, 2001, an agreement in principle was reached that was supported by most, but not all, parties to the case. That agreement is as follows.

II. *PROPOSED SETTLEMENT*

A. Rate Provisions Effective October 1, 2002

1. Effective October 1, 2002, and applicable to all non-residential rate classes other than those receiving service under Rate Class SGS-ND, [10] the Competitive Transition Charge ('CTC') rates in effect as of September 30, 2002, which reflect costs that had been removed from the supply component of rates and added to the delivery component in Docket No. 99-163, shall be moved from the delivery component of rates and reassigned back to the supply component of rates. The CTC rate components in effect on September 30, 2002, by applicable service classification and using the same demand, energy on-peak/off-peak, and seasonal factors, shall each be added to the comparable supply rates and no longer carried on the tariff leafs as separate line items, so there will be a zero net change in revenues.

2. Effective October 1, 2002, and applicable to all non-residential rate classes other than those receiving service under Rate Class SGS-ND, the rate factors embedded within the distribution component of rates that reflect nuclear decommissioning costs included in the rates established in Docket No. 99-163 (as reflected in Appendix D, Attachment 2 workpapers to the Compliance filing of September 15, 1999 in that proceeding) shall be removed from the distribution component of rates and these same rate factors, by applicable service classification and using the same demand, energy on-peak/off-peak, and seasonal factors, shall be added to the comparable supply rates, so there will be a zero net change in revenues.

3. Effective October 1, 2002, and applicable to all non-residential rate classes other than those receiving service under Rate Class SGS-ND, the 'returning customers' rule set forth in Delmarva's current retail tariff established in Docket No. 99-163 shall be modified so that a retail customer who has obtained its supply from an Electric Supplier and who returns to Delmarva's Standard Offer Service on or after October 1, 2002, shall be obligated to pay for its supply charges pursuant to either Delmarva's Market Priced Supply Service ('MPSS') as modified and attached hereto (Attachment 1), or, if mutually agreeable in each parties' sole discretion, a negotiated market price. A customer who is served under the MPSS shall be eligible to switch to an Electric Supplier without a minimum stay requirement other than the standard requirement that a switch to an Electric Supplier take place on the customer's next meter read date after appropriate notice of a switch is provided to Delmarva by the Electric Supplier. Any non-residential rate class customer who takes supply from an Electric Supplier and who returns to Delmarva's Standard Offer Service on or before September 30, 2002, however shall have the option of paying Delmarva's Standard Offer Service frozen supply rate in which case it shall be obligated remain as such for a minimum of 12 months before being permitted to enroll with an Electric Supplier.

4. The rate modifications set forth in paragraphs 1 and 2 above shall remain in effect (*i.e.*, shall be 'frozen') from October 1, 2002, through September 30, 2003, subject only to changes pursuant to section C.1, hercin.

B. Rate Provisions Effective October 1, 2003

1. Effective October 1, 2003, and applicable to all non-residential customers other than those receiving service under Service Classification SGS-ND, the supply components of rates shall be increased such that the supply rate components in conjunction with the supply rate increases pursuant to section II.A.2. are equal to 103% of: 1) the supply rates as in effect as of October 1, 2002, minus 2) the supply rate component increases pursuant to section II.A.2.

2. Effective October 1, 2003, and applicable to residential customers and non-residential customers receiving service under Service Classification SGS-ND, the rate embedded within the distribution component of rates that reflects nuclear decommissioning costs included in the rates established in Docket No. 99-163 (as reflected in Appendix D, Attachment 2 workpapers to the Compliance Filing of September 15, 1999 in that proceeding) shall be removed from the distribution component of rates. Effective on the same date and for the same customers, an increase of 3% shall be applied to each of the supply component rates.

3. Effective October 1, 2003, and applicable to residential customers and non-residential customers receiving service under Service Classification SGS-ND, the 'returning customers' rule established in

Docket No. 99-163 set forth in Delmarva's current retail tariff shall be modified so that such a retail customer who has obtained its supply from an Electric Supplier and who returns to Delmarva's Standard Offer Service on or after October 1, 2003, shall be obligated to remain on Delmarva's Standard Offer Service for a minimum period of 12 months before being permitted to re-enroll with a third-party supplier.

4. The rates in effect as of October 1, 2003 shall remain in effect until May 1, 2006, subject to change only pursuant to the provisions of section C below.

C. *Exceptions to the Rate Freeze.*

1. Nothing in this Settlement shall be deemed to be a waiver of Delmarva's rights under 26 *Del. C.* § 1006 to seek the recovery of extraordinary costs as the Commission may, in its discretion, determine during the transition period established by statute. Notwithstanding the above sentence, Delmarva agrees not to seek a change in residential retail rates in the fourth year of the existing retail rate freeze established in Docket No. 99-163 to reflect increased supply costs pursuant to the so-called 'Side Letter Agreement' section 3(G).

2. Between October 1, 2003, and May 1, 2006, Delmarva may make a filing seeking the recovery of extraordinary costs as the Commission may, in its discretion determine. The Settling Parties reserve all rights to protest or take any position on any such filing.

3. In addition to any other right set forth in this Agreement and notwithstanding any other provision that would otherwise limit the ability of Delmarva to file for a rate change, Delmarva shall have the right to file to change its Transmission components of rates to reflect the then-applicable Transmission charges incurred by Delmarva pursuant to Federal Energy Regulatory Commission ('FERC')-approved transmission charges of the PJM Interconnection, LLC., or successor organization ('PJM'). The proposed Transmission components of retail rates shall go into effect within 30 days of filing, subject to refund and Commission review in a docketed proceeding. In such a retail proceeding, no Settling Party will raise and all Settling Parties participating in the proceeding will oppose any positions taken that such a rate change is inappropriate or should be offset in part or in whole due to changes in other costs, revenues, or other factors (including cost of capital); provided, however, that nothing herein shall restrict a Settling Party from taking the position that the proposed rate change should be offset in whole or in part because Delmarva, in its role as a transmission owner, is earning incremental revenue from parties (including affiliated entities and retail customers) other than Delmarva under the FERC-approved transmission charges; and provided, further, that the proceeding shall consider, and all Settling Parties reserve their rights with respect to, whether to reset transmission rates based on billing determinants and methodologies that correspond to the billing determinants and methodologies used by PJM to charge Delmarva for transmission. The right to file for a rate increase is limited to one filing with an effective date on or after October 1, 2003, and before May 1, 2006. Nothing herein shall be deemed to restrict any Settling Party's rights to intervene in and take any position with respect to an FERC proceeding relating to the transmission charges of PJM or its successor.

4. In addition to any other right set forth in this Agreement and notwithstanding any other provision that would otherwise limit the ability of Delmarva to file for a rate change, Delmarva shall have the right to file to change its Ancillary components of rates to reflect the then-applicable Ancillary charges billed to Delmarva by PJM or successor organization. The proposed Ancillary components of retail rates shall go into effect within 30 days of filing, subject to refund and Commission review in a docketed proceeding. In such a retail proceeding, no Settling Party will raise and all Settling Parties participating in the proceeding will oppose any positions taken that such a rate change is inappropriate or should be offset in part or in whole due to changes in other costs, revenues, or other factors (including cost of capital); provided, however, that nothing herein shall restrict a Settling Party from taking the position that the proposed rate change should be offset in whole or in part because Delmarva, in its role as a transmission owner providing transmission-related ancillary services, is earning revenue from parties (including affiliated entities and retail customers) other than Delmarva for the ancillary services it provides. The right to file for a rate increase is limited to one filing with an effective date on or after October 1, 2003, and before May 1, 2006. Nothing herein shall be deemed to restrict any Settling Party's

rights to intervene in and take any position with respect to an FERC proceeding or any PJM process (including but not limited to processes involving PJM's Market Monitoring Unit) relating to the ancillary charges of PJM or its successor.

5. Nothing in the existing rate freezes as established in Docket No. 99-163 nor established herein shall be deemed to preclude Delmarva from filing for rates that would be applied to new lighting services or products, back-up or emergency services for distributed generation services, dual-feed services, advanced metering services, or other similar services not currently tariffed and made available as an optional service to customers; provided, however, that there would be no change in the transmission and distribution rates established herein as applied to customers who do not elect to take such optional services; and provided further that it is recognized that while a distributed generation service may be optional from a customer perspective, there may be a mandatory requirement for back-up or emergency services associated with such distributed generation services.

6. Nothing in the existing rate freezes as established in Docket No. 99-163 nor established herein shall be deemed to preclude Delmarva from filing or any Settling Party from petitioning the Commission for revenue neutral rate design proposals that would reflect changes made by PJM or FERC in the definitions and functionalization of transmission and distribution facilities. For purposes of this paragraph, a revenue neutral rate design proposals shall be revenue neutral to Delmarva in the aggregate for all customer classes and revenue neutral within each customer class, *i.e.*, no shifts in revenue responsibility between customer classes. Any such filings shall be subject to Commission review, no Settling Party waives any rights to oppose such filings, and the proposed modifications shall not go into effect unless approved.

7. Nothing in the existing rate freezes as established in Docket No. 99-163 nor established herein shall be deemed to preclude Delmarva from filing for changes to its Rules and Regulations set forth in its existing Delaware retail electric tariff. Any such filings shall be subject to Commission review, no Settling Party waives any rights to oppose such filings, and the proposed modifications shall not go into effect unless approved.

8. The rate freezes established herein shall not apply with respect to the contracts described in section II.F. below.

9. The rate freezes established herein shall not apply with respect to changes that may be proposed by Delmarva or any other party to the size of the credits payable pursuant to or the provisions of the Peak Management Rider or to an alternative load management program that may be developed for larger commercial and industrial customers.

10. Nothing herein shall be deemed to preclude any Settling Party from petitioning the Commission to modify charges in the MPSS to reflect more accurately market costs of the Company's provision of such service.

D. *Standard Offer Service.*

1. The Settling Parties agree that the Commission should find, pursuant to 26 *Del. C.* §§ 1006(a)(2) and 1010(a)(2), that: Delmarva shall be the Standard Offer Service supplier for Delmarva service territory until May 1, 2006; the price increases set forth above for the supply component of the Standard Offer Service is representative of the regional wholesale electric market price, plus a reasonable allowance for retail margin; and the next periodic review of this price will occur on or about May 1, 2006, in conjunction with a process intended to result in the selection of a Standard Offer Supplier on and after May 1, 2006.

2. The Settling Parties recognize and agree that it is within the purview of Delmarva's management to acquire the necessary supply resources to meet its obligations to provide Standard Offer Service through May 1, 2006, and Delmarva, if it deems appropriate in its sole discretion, may meet such obligations by means of a full or partial requirements contract with an affiliated entity, or otherwise.

3. Nothing herein shall be deemed to imply that Delmarva is assuming any supply obligation for Standard Offer Service or otherwise beyond May 1, 2006.

E. *Effects of Settlement on Rates Prior to October 1, 2002, and October 1, 2003.*

*9 Nothing herein is intended to provide any rights beyond those set forth in present law and applicable orders of the Commission to change rates prior to the end of the rate freeze periods specified in the settlements in Docket No. 99-163, which provide for rate freezes extending through September 30, 2002, for non-residential customers and through September 30, 2003, for residential customers.

F. *Contracts for Certain Large, Interruptible Customers.*

1. a) BOC and Delmarva agree to terminate, with prejudice, the litigation in Docket No. 00-653 without a final decision being made by the Commission in that proceeding, subject to the following conditions: i) with respect to the period of April 1, 2000 through March 30, 2001, BOC shall pay the amounts withheld (estimated to be in the range of $662,000 to $679,000) from the Delmarva portion of its bills for such period and no late payment charges shall be imposed with respect to such amounts; ii) with respect to the period of April 1, 2001 through September 30, 2002, Delmarva shall bill BOC pursuant to the GS-T service classification rates (as set forth in Tariff Leaf No. 47 and applying the provisions of the GS-T service classification Leaf Nos. 71-72, paragraphs A, C, E, F, G, H, I, J, K and L), except that the Distribution portion of such rates shall be equivalent to rates set forth in Q service classification rates (as set forth in the 'Delivery Service Charges on Tariff Leaf No. 48 for firm (750 Kw) and controllable load (all other); iii) with respect to any payments made by BOC since April 1, 2001, that are in excess of the amounts billed or to be billed pursuant to subparagraph II.F.1.a)ii), Delmarva shall refund the difference to BOC and no interest shall be paid with respect to such refund amounts; and iv) such provisions shall be part of a Special Interim Contract between BOC and Delmarva. Delmarva and BOC agree that BOC will have no rights or claims to receive service under Q service classification at any time in the future.

b) The amounts to be paid by BOC under subparagraph II.F.1.a)i) and to be refunded by Delmarva under subparagraph II.F.1.a)iii) may be netted for administrative convenience, if mutually acceptable.

c) For the period between the date on which the Commission approves this Settlement and October 1, 2002, the Special Interim Contract will provide for a hybrid service that will apply such that certain provisions relating to, for example, the events giving rise to the right to call for interruptions, notice periods for interruptions and similar requirements applicable herein to the Distribution service shall be as set forth in the Q service classification, while the non-Distribution services of the hybrid service, including rates, computations of demand factors, minimum charges, and similar items shall be as set forth in the GS-T service. Specifically, paragraphs E, F, H, I, K, L, M., P, Q, and R of the Q service classification tariff leaves shall be applicable to the Distribution component of service, except that (1) the charges applied in paragraph L.1 and the penalties associated with paragraph M shall be deemed to reference the charges applicable under the GS-T service classification and (2) for purposes of paragraph K, BOC shall be deemed to receive only the Distribution service from Delmarva and requests for load reductions shall only be made to prevent or minimize an emergency operating condition on Delmarva's electric system. For all other components of service, the provisions of paragraphs A, C, D, E, F, G, H, I, J, K, and L of the GS-T service classification shall apply. BOC recognizes that an interruption of Distribution service will also result in an interruption of other services.

*10 d) No later than 90 days prior to October 1, 2002, and sooner if convenient for both parties, BOC and Delmarva shall enter into good faith negotiations in an attempt to reach a mutually-acceptable contract for service on and after October 1, 2002. It is recognized that any such contract, if not in full compliance with a standard tariffed service, will be subject to the requirements of Delmarva's Negotiated Contract Rate service, including the requirements that: i) BOC has an economic competitive alternative to full or partial service from the Company's standard tariff rates; ii) BOC is likely to select such an alternative if Delmarva does not provide a negotiated contract rate offer; and iii) BOC will provide net revenues above Delmarva's incremental costs to provide service. Neither BOC nor Delmarva represent that good faith negotiations will necessarily be successful. BOC recognizes that, in the event that BOC and Delmarva do not reach a mutually satisfactory Negotiated Contract Rate agreement, each acting in its sole discretion, or if such a Negotiated Contract Rate agreement is reached but is not permitted to become effective by the Commission, BOC will accept service from Delmarva on and after October 1, 2002, provided and billed under Delmarva's GS-T service; provided, however,

that in such event, BOC shall have the right, to the extent permitted by tariff, to elect the Peak Management Rider, or other load management provision that is a tariffed service; and provided further that, in such event, BOC shall also have the right to obtain load management services or credits from third party marketers.

e) Notwithstanding the existing 'returning customer' rule in Delmarva's tariff, as of the later of approval by the Commission of this settlement or January 1, 2002, and for one-time only, BOC shall have the right to obtain its transmission, ancillary, and supply services from a competitive supplier.

2. Occidental Chemical Corporation ('OxyChem') is an existing Q customer with a contract for which Delmarva has given a notice of termination effective as of November 1, 2002. No later than 90 days after this Settlement is approved, and sooner if convenient for both parties, OxyChem and Delmarva shall enter into good faith negotiations in an attempt to reach a mutually-acceptable agreement for service on and after October 1, 2002. It is recognized that any such agreement, if not in full compliance with a standard tariffed service, will be subject to the requirements of Delmarva's Negotiated Contract Rate service, including the requirements that: i) OxyChem has an economic competitive alternative to full or partial service from the Company's standard tariff rates, including, *e.g.*, fuel switching, facility relocation or expansion, partial or complete plant production shifting, or potential physical bypass; ii) OxyChem is likely to select one or more of such alternatives if Delmarva does not provide a negotiated contract rate offer; and iii) OxyChem will provide net revenues above Delmarva's incremental costs to provide service. Neither OxyChem nor Delmarva represent that good faith negotiations will be successful. OxyChem recognizes that in the event that OxyChem and Delmarva do not reach a mutually satisfactory Negotiated Contract Rate agreement, each acting in its sole discretion, or if such a Negotiated Contract Rate agreement is reached but is not permitted to become effective by the Commission, OxyChem will accept service from Delmarva on and after November 1, 2002, provided and billed under Delmarva's GS-T service; provided, however, that in such event, OxyChem shall have the right, to the extent permitted by tariff, to elect the Peak Management Rider, or other load management provision that is a tariffed service; and provided further that in such event, OxyChem shall also have the right to obtain load management services or credits from third party marketers. The Settling Parties agree that OxyChem will have no rights or claims to receive service under Q service classification at any time in the future after November 1, 2002.

3. CitiSteel USA, Inc. ('CitiSteel') is an existing Q customer with a contract with an initial term expiring in May 2004. Delmarva and CitiSteel shall enter into an agreement (the 'Replacement Contract') on or before June 1, 2002, that will terminate the service under the Q service classification as of September 30, 2002, but, for the period between October 1, 2002, and the termination date of the existing contract, will provide rates, terms and conditions that are the same as the currently existing contract and Q service classification as they currently exist. The Replacement Contract, which may in the form of amendments to the existing contract or a completely new contract, will be filed with the Commission and the Settling Parties will either support its effectiveness or not oppose its becoming effective on grounds that such Replacement Contract imposes no incremental costs beyond those presently incurred by Delmarva under the existing contract. The Replacement Contract will not be assignable except upon written consent by Delmarva, which consent shall not be unreasonably withheld. Contingent on the execution of the Replacement Contract, the Settling Parties agree that CitiSteel will have no rights or claims to receive service under Q service classification at any time in the future after October 1, 2002.

4. Delmarva and BOC recommend that the Commission explicitly waive or eliminate any requirement as set forth in Order No. 2852, dated June 9, 1987, that Delmarva develop a tariffed service that would be available to customers similarly situated to BOC and further explicitly find that such waiver or elimination of such requirement also be found to apply with respect to BOC.

5. Notwithstanding any other provision of the Settlement, the provisions of this subsection II.F. shall become effective as of the date the Commission approves this Settlement.

G. Corporate Presence

*11 Applicants agree that for the next 5 years, Conectiv Power Delivery's operational headquarters will remain in Delaware, that there will be a significant senior management presence working in offices in Delaware. Applicants agree that for the next six years, Conectiv will make contributions to charities in Delaware at levels comparable to its historic levels. The Settling Parties recognize that, pursuant to agreements not jurisdictional to this Commission, existing union contracts will be honored, which contracts include specific provisions relating to the preservation of union jobs for employees represented by the IBEW locals and relating to severance and benefits. In addition, Applicants agree within 30 days after closing to make a one-time contribution to Murex Investments in the amount of $750,000, which contribution may be in the form of an investment or a gift, at Applicants' discretion; provided, however, that the contribution shall be in a form that would trigger a matching contribution of federal or Small Business Administration funds to the extent such funds are available. Such contribution shall be conditional on an obligation on the part of Murex to expend such contribution for job training or small business development within Delmarva's Delaware service territory and on Murex making its best efforts to expend the matching contribution from the federal Small Business Administration for job training or small business development within Delmarva's Delaware service territory.

H. *Merger-Related Costs.*

1. Applicants agree not to seek recovery in future rates of Delaware's portion of: (1) merger transaction costs, estimated to be $46 million, as shown on page 33 of the merger Form U-1 on file with the U.S. Securities and Exchange Commission; (2) the merger acquisition premium paid by Pepco; (3) the costs of any termination or severances that occur within an eighteen month period following closing of the merger, including merger-related severances or terminations that are agreed to by Applicants within the eighteen month period that becomes effective only after the close of that period.

2. With respect to merger-related transition costs other than termination and severance costs, the Settling Parties recognize that defining the categories of such costs precisely at this point in time is difficult. It is presumed that costs incurred more than 18 months after closing are not merger-related. It is further recognized that, because regulated rates are frozen until May 1, 2006, with certain specified exceptions, the potential recovery of merger transition costs will be limited. It is therefore the Settling Parties understanding that in future rate cases, normal ratemaking principles and presumptions will operate such that Delmarva has the burden of proof that its rates are just and reasonable and reflect test period expenses that are properly included in its revenue requirement computations; other Settling Parties reserve their rights to assert that such costs are merger-related and should not be recoverable.

3. Applicants agree that if the merger does not close, Delmarva will not seek to recover in rates any termination fees or other fees, costs, or expenses incurred with respect to the merger.

I. *Renewable Resources, Conservation Programs and Advanced Metering.*

1. Applicants agree that within 60 days after closing a one-time contribution of $200,000 shall be made to an organization to be designated by the Staff and DPA for the promotion of renewable resources in Delaware. In addition, Delmarva will include as a bill insert in one month of billing within the first year after closing, information to customers advising them of the existence of such organization and providing the information necessary to permit customers to submit contributions directly to such organization. The text of such billing information shall be previewed with the Staff and DPA prior to its inclusion as a bill insert.

2. Applicants agree to participate in a working group that will be charged with the responsibility to identify any cost-effective demand-side management or conservation programs and develop specific program recommendations.

3. Delmarva agrees to work in good faith with Staff and other interested parties (whether part of this proceeding or not) to initiate a pilot program for approximately 250 residential or small

commercial customers that would test the appropriateness of larger-scale initiatives or offerings with respect to real-time metering or advance-pay metering, or other similar metering technologies.

J. Customer Guarantees.

1. Applicants proposed nine service level guarantees ('SLGs') in this proceeding. The Settling Parties agree that the review of five of those SLGs and any modifications to be made with respect to those five SLGs should be made in other pending cases before the Commission. Specifically, the proposed SLGs relating to telephone service factor and abandonment rate shall not be reviewed or approved in this proceeding, but such matters are to be addressed in Docket No. 99-328; the proposed SLGs relating to the CAIDI statistic, SAIDI statistic, and poor performing circuits shall not be reviewed or approved in this proceeding, but such SLGs are to be addressed in Regulation Docket No. 50. Delmarva further agrees that it shall not assert in Regulation Docket No. 50 that the Commission lacks the power to establish a poor performing circuit standard that includes a provision providing for a penalty if such standard is violated; provided, however, Delmarva retains all rights to argue that no such penalty is appropriate or lawful or imposed consistently with its due process rights and all Settling Parties, including Delmarva, retain their rights to argue on the merits as to what standard, if any, should be established.

2. With respect to the SLG relating to 'Appointments Kept,' the Settling Parties agree that the Commission should approve such SLG as filed by Delmarva, with the modification that there will be no exemptions for rescheduling appointments unless such rescheduling occurs no later than the close of business on the last business day prior to the date of the appointment. With respect to the SLG relating to 'New Residential Customer Installations,' the Settling Parties agree that the Commission should approve such SLG as filed by Delmarva, except that the guarantee will be extended to cover re-energizing existing services at the same premise. It is understood that Delmarva will establish an internal goal for such re-energizing to occur within 3 business days, but the guarantee will apply only if there is a failure to re-energize within 10 days. With respect to the SLG relating to 'Bill Accuracy,' the Settling Parties agree that the Commission should approve such SLG as filed by Delmarva. With respect to the 'Outage Restoration' SLG, the Settling Parties agree that the Commission should approve such SLG as filed by Delmarva, except that there will be a $50 payment for each additional 24 hours or portion thereof of an outage extending beyond 48 hours.

3. Nothing in this subsection II.J., shall be deemed to supersede or limit any existing right that a customer may have with respect to complaints, bill adjustments, or other processes involving customer service.

K. Competitive Supplier Provisions.

1. Delmarva agrees that in the event a competitive supplier proposes to the appropriate entities a modification to regional standards regarding the 867HU transaction to include LDC rate code and profile group as optional fields, then Delmarva will support such a modification; and within a commercially reasonable time after the implementation of such a regional modification, Delmarva will modify its 867HU transaction processes to permit such information to be exchanged with an EDI-capable counterparty.

2. Subject to the caveats and exclusions herein, and applicable to customers who, prior to June 20, 2000, entered into Peak Management Rider ('PM Rider ') contracts for periods in excess of one year Delmarva will eliminate the provision in the PM Rider that requires a PM customer to purchase its electricity from Delmarva. With such elimination, such customers will be able to choose any Electric Supplier, who will be obligated to purchase 'unforced capacity' (as that term is defined by PJM, or a comparable successor term if so redefined by PJM) sufficient to meet the customer's unrestricted Peak Load Contribution (as annually computed by Delmarva including the add back of the Active Load Management ('ALM') amounts), energy, and transmission and ancillary services, without the customer terminating its PM Rider contract with Delmarva. The Settling Parties recognize that the intent of such modifications is to allow the customer to obtain its electric requirements from an Electric Supplier while continuing to receive the PM Rider payments from Delmarva and for Delmarva to retain the benefits that PJM ascribes to ALM. In order to be eligible for this treatment, the customer and Electric Supplier must have a contract in place (and the Electric Supplier must so certify to Delmarva) that provides the

customer with specific notice that if PJM reduces or eliminates the benefits of ALM to Delmarva due to the customer's enrollment with the Electric Supplier, then the PM Rider contract will be subject to termination at Delmarva's sole discretion on 30 days notice. In addition, the PM Rider will be modified to provide a penalty up to the total amount of Peak Management credits paid by Delmarva to the customer within a given year in the event that Delmarva calls for an interruption or reduction of load consistent with the PM Rider and the customer fails to comply to the extent required and Delmarva will have the right to terminate the PM Rider contract for a failure of a customer to comply. Nothing herein shall be deemed to affect other provisions that may be in a contract between Delmarva and a customer who is receiving PM Rider credits. The PM Rider minimum contract term shall also be modified from a calendar year basis to any period of 12 months and year-to-year thereafter, subject to termination on 60 days' notice by either party. For PM Rider contracts with an effective date beginning on or after July 31 of a given year, the minimum period will be 12 months with a maximum period extending through the end of the next subsequent PJM planning period (*e.g.*, an August 2002 contract could extend through May 2004), and year-to-year thereafter, subject to termination on 60 days' notice by either party.

L. *Interval Customer Data.*

*12 Delmarva agrees to make best efforts to develop and implement within 9 months after the merger closes (but in no event later than 12 months), a web-based mechanism to permit the transfer, without manual intervention on the part of Delmarva, of historic interval data for its Delaware retail customers that have interval recording devices that record such interval load. Nothing herein shall be deemed to waive any obligations on the part of a user of such data to comply with requirements of the Commission with respect to receipt of customer information. The web-based data will be periodically updated, but no more frequently than once a quarter. Nothing herein shall be deemed to modify existing warranty limitations and provisions in Delmarva's Supplier Agreement regarding data provided to Electric Suppliers. The fees for interval data shall cease no later than 12 months after the merger closes. Delmarva has stated an intent to terminate its manual process at some point after the web-based mechanism is in operation; Settling Parties neither support nor oppose such intent by Delmarva and reserve their rights.

M. *Reliability Provisions.*

1. Delmarva has stated that Delmarva currently meets all current PJM and MAAC reliability criteria through 2006, assuming that its planned transmission construction projects are completed. Unless circumstances change that eliminate the need for such projects or accelerate or postpone the need for such projects, Delmarva agrees to construct those planned projects as scheduled, and, in the event circumstances do change, Delmarva will consult with Staff and DPA as to resultant changes to its project schedules prior to modifying its plan.

2. Delmarva also agrees to construct by May 2008, projects known as the: Piney Grove Autotransformers; the Mt. Hermon — North Salisbury project; and the Todd-Vienna 69 Kv bus work. The in-service dates set forth in this subsection are subject to change if circumstances change on the peninsula such that need for such projects is accelerated, eliminated, or postponed. In the event circumstances do change, Delmarva will consult with Staff and DPA as to resultant changes to its project schedules prior to modifying its plan.

N. *Congestion Provisions.*

1. The Settling Parties agree that it is their intent to establish cost-effective mechanisms that will operate to limit congestion hours on the Delmarva Peninsula to the levels at or below the prescribed thresholds outlined herein. This subsection II.N. shall become effective on an interim basis as of the date that the Commission issues a final order approving this Settlement and shall become final upon closing of the merger; provided, however, that if the merger is terminated and does not close, this subsection II.N. shall be eliminated and have no force or effect.

2. Delmarva agrees to accelerate the 2007 planned in-service date of the Red Lion — Milford-Indian River 230 Kv transmission line to May 2006. Prior to any changes to this schedule for any reasons, Delmarva will consult with Staff and DPA.

3. For the period beginning on January 1, 2002, Delmarva will track, using the 'Off-Cost Operations' data on the PJM web-site, the number of hours of congestion on Delmarva's on-peninsula transmission system.

4. a) The provisions of this subsection II.N.4 shall be applicable in the event that the sum of the hours of Off-cost Operations for all of Delmarva's on-peninsula transmission facilities (non-facility specific) exceeds the applicable threshold for the annual number of hours during which one or more of Delmarva's on-peninsula transmission facilities are constrained. The applicable annual aggregate number of hours (the 'triggering event thresholds') are as follows: 1000 hours in calendar-year 2002, 850 hours in calendar year 2003, 700 hours in calendar year 2004, 600 hours in calendar year 2005, and 200 for the period January 1 — April 30, 2006) (with such hours excluding Off-cost Operations attributable to generation or transmission forced outages and excluding generation or transmission construction). [11] **In calculating the hours toward a triggering event threshold Delmarva shall include each hour where a transmission facility maintenance outage is listed on PJM's Off-cost Operations, except that certain hours may be excluded as follows: if Delmarva, which has the burden of presentment and proof with respect to any such showing, can demonstrate that there is a concurrent forced generation outage and Delmarva had scheduled with PJM a transmission maintenance outage prior to the forced generation outage and that, in the absence of such forced generation outage, the scheduled transmission maintenance outage would not have caused congestion for particular hours, then such hours shall be excluded.**

*13 b) *Step 1 analysis.* Within 60 days of exceeding such triggering event thresholds, Delmarva shall be required to prepare an analysis of the economic impacts of the congestion and the economic impacts of transmission projects that would alleviate this congestion to determine cost-effective solutions that would reduce the level of congestion to below the applicable triggering event threshold. The analysis, which will be provided to Staff, would seek to identify the most cost-effective solution irrespective of the number of hours of congestion that would be relieved, *e.g.*, if there were a triggering event where the number of hours exceeded the threshold by 100 hours, but the most cost-effective solution involved construction that would relieve 500 hours of congestion, that 500 hour solution would be implemented pursuant to the mechanisms below. The evaluation would include an analysis of whether the construction of additional Delmarva transmission facilities has a lesser cost than solutions that could be implemented by other market participants.

c) For purposes of Step 1 of this analysis, the determination of whether a solution is 'cost-effective' shall consider as a 'benefit' only the congestion charges incurred by Delmarva during the same period that triggered the analysis that would have been avoided if the identified facility(ies) had been in service (the 'Incremental Avoided Congestion Charges'). [12] For purposes of this 'cost-effective' analysis, the costs considered will be equal to the net of Delmarva's total estimated costs of construction minus any 'carry-forward net FTR credits' (as defined below) multiplied by Delmarva's carrying cost rate and, for future ratemaking purposes, the actual capitalized rate base costs of construction shall be reduced by the amount of any carry-forward net FTR credits applied. Under no circumstance would rate base or revenue requirements be increased by any negative carry forwards.

d) *Step 2 Analysis.* In the event that the Step 1 analysis fails to identify a cost-effective solution, a Step 2 analysis would be made, which will add to the Step 1 benefit an amount equal to a ratio of the hours of congestion in excess of the applicable triggering event threshold over the total hours of congestion multiplied by any net positive difference between FTR credits appearing on Delmarva's PJM bills and Aggregate Congestion Costs. [13] For future ratemaking purposes, the actual capitalized rate base costs of construction shall be reduced by the amount of any carry-forward net FTR credits applied. Under no circumstance would rate base or revenue requirements be increased by any negative carry forwards.

*14 e) In the event that the cost-benefit analysis described above under Step 1 or Step 2 results in a positive benefit (*i.e.*, is cost-effective), Delmarva will construct such project.

f) *Step 3 Procedure.* In the event that the cost-benefit analysis described above does not result in a positive benefit (*i.e.*, costs are in excess of benefits computed as set forth above), Step 3 will be implemented. Delmarva will seek additional contributions in aid of construction (including tax effects, if applicable) from other market participants. No other entity will be required to contribute to the capital costs of constructing any additional Delmarva transmission facilities that are constructed under the provisions hereof, but if contributions are received (net of tax effects, if applicable), that would eliminate the amount by which costs are in excess of benefits under the Step 1 and 2 analyses, then such project shall be deemed to be cost-effective and Delmarva will construct such project. Delmarva's rate base and associated revenue requirement will not include capital costs contributed by third parties under this provision or the amount of any carry-forward net FTR credits applied. Under no circumstance would rate base or revenue requirements be increased by any negative carry forwards.

g) For each year 2002 through May 2006, the following computations shall be made: i) in the event that a triggering event threshold has been exceeded; ii) no cost-effective project is identified pursuant to the Step 1, Step 2 and Step 3 analyses above; and iii) during the same period there is a difference between FTR credits appearing on Delmarva's PJM bills minus Aggregate Congestion Charges; then iv) Delmarva shall take such difference (whether positive or negative) and separately reserve for future construction an amount equal to a ratio of the hours of congestion in excess of the applicable triggering event threshold over the total hours of congestion multiplied against any difference between FTR credits appearing on Delmarva's PJM bills and Aggregate Congestion Charges for the same period. These amounts will be the 'carry-forward net FTR' credits (if positive) or debits (if negative). To the extent that, in a given year, there is a net credit position (after offsetting any prior year carry-forward net FTR debits), that net credit that will be applied as an offset to the estimated costs for a project identified in a subsequent year to determine whether a project in such subsequent year is cost-effective. To the extent a carry-forward net FTR credit is applied to construct a project that would otherwise not be cost effective, the rate base effects of that project shall be reduced by the amount of carry-forward net FTR credits applied. To the extent any carry-forward net FTR credits exist as of May, 2006, such amounts shall be earmarked for Delmarva's capital budget plan for post-2006 periods and the rate base effects of capital projects constructed with such carry-forward net FTR credits shall be reduced by the amount of carry-forward net FTR credits applied. In the event that a negative carry-forward balance exists as of May 2006, that balance shall be zeroed-out and under no circumstance shall rate base or revenue requirements be increased by any such negative carry-forward balance.

***15** h) Attached hereto (Attachment 2) and incorporated herein are four (4) examples of how the congestion provisions herein will work.

i) Delmarva will file with the Staff semi-annual reports on or before each August 1 (for the period January — June) and on or before February 1 (for the previous calendar year), which reports shall contain the FTR, congestion costs, congestion hours and other data applicable to the requirements in this subsection II.N.

5. In the event that a cost-effective project is identified that should result in Delmarva constructing additional transmission facilities on the peninsula pursuant to the mechanisms described in the preceding paragraph N.4, and if Delmarva fails to initiate the construction process within sixty (60) days of the identification of said cost-effective project and complete such construction as soon as practicable, using prudent utility practices, then Delmarva shall be obligated to make funds available to third parties for constructing such facilities; provided, however, that such funds shall not exceed the net positive difference between FTR credits appearing on Delmarva's PJM bills and the Aggregate Congestion Charges multiplied by the ratio of the hours of congestion in excess of the applicable triggering event threshold over the total hours of congestion plus any carry-forward net FTR credits. Delmarva's rate base and associated revenue requirement with respect to such projects constructed by others will include only the capital costs contributed hereunder by Delmarva and will not include any costs incurred by third parties under this provision.

6. ODEC, as a signatory herein, has agreed to complete two planned construction projects located on the South Peninsula (*i.e.*, installation of additional capacitor banks on the A&N Electric Cooperative distribution system to improve the power factor of ODEC's peak load to unity or slightly leading; and establishing a new tap point on the Oak Hall-Tasley circuit 6778 and transferring some of ODEC's load presently served from Hallwood-Oak Hall circuit 6790).

7. Irrespective of the provisions of subsection N.4. and irrespective of whether any of the thresholds are exceeded resulting in a triggering event, Delmarva agrees that if ODEC identifies a project that, after Delmarva's study of the costs and benefits of such project, is determined to provide a cost-effective solution for congestion costs incurred by Delmarva, then Delmarva will construct the project; provided, however, that nothing herein shall be deemed to limit Delmarva's consideration of alternative projects that could relieve such congestion within a comparable time period and provide similar benefits, including committed expansions of generators on the peninsula by third parties, Delmarva's already planned transmission facilities or alternative projects.

8. The Settling Parties are aware that PJM has initiated a process that is expected to lead to a proposal for providing incentives and other mechanisms, which may include cost sharing mechanisms that may conflict with those established herein, to encourage the construction of new transmission facilities to relieve congestion in a cost-effective manner. It is agreed by the Settling Parties that, to the extent that a PJM proposal approved by FERC supersedes or conflicts with any of the actions that must be undertaken by Delmarva or other Settling Parties pursuant to this Settlement, then Delmarva shall make a filing for Commission approval of any changes to this Settlement and Delmarva shall have the burden of proving that such a change is necessary in light of the order of the FERC. In such a proceeding, all other parties reserve their rights to oppose such filing and to take positions in such Commission proceeding in their own individual interest. The superseded or conflicting provisions herein, as determined by the Commission and subject to appeal, shall be of no force of effect and severable from the remaining provisions of this Settlement, which shall continue to be effective.

O. *Miscellaneous.*

1. As of the date on which no customer is provided service under the Q service classification, which is expected to be November 1, 2002, or sooner, the Q service classification tariff leafs shall be cancelled and removed from Delmarva's Delaware retail electric tariff.

2. The Settling Parties agree and will recommend that the Commission accept pursuant to 26 *Del. C.* § 1006(a)(2) d., a filing to be made by Delmarva on or before March 1, 2002, in which Delmarva will include schedules demonstrating its overall rate of return based on cost of service data, with a proposal that no rate changes with respect to its regulated services be implemented other than those set forth herein. The Settling Parties shall have the right to review such filing and schedules, except that no recommendation will be made by them to establish new rates or rate changes other than those set forth herein, and the Settling Parties shall oppose or not support any efforts by other entities who might propose rate changes other than those set forth herein.

3. On or before September 1, 2005, Delmarva will file a class cost of service study in sufficient detail to permit a review and determination of the justness and reasonableness of its regulated rates, with any resulting rate changes to take place no earlier than May 1, 2006.

4. Each Settling Party reserves the right to petition the Commission to reopen this proceeding for the purpose of substituting the terms and conditions of this Settlement with the terms and conditions of a different settlement entered into by Delmarva in Maryland. Such right shall be exercisable only within 30 days of the filing of such settlement made in Maryland and will require the complete replacement of this Settlement with the other settlement, with modifications only to the extent necessary to reflect particular terms used in Delaware that differ from similar terms in other jurisdictions. It is understood by the Settling Parties that the provisions of this Settlement are non-severable and, thus, any substitution of another settlement entered into by Delmarva in Maryland will make null and void all provisions of this Settlement.

5. Contemporaneously or as soon as reasonably practicable, Delmarva shall provide Staff a copy of any initial filing made by Delmarva or PJM before the FERC that would reset transmission rates.

6. In the event that the merger has not closed by June 30, 2002, the Settling Parties agree that:

*16 a) The provisions of subsections II.A.1, 2, and 3, shall be effective as of October 1, 2002;

b) Delmarva shall be the Standard Offer Service supplier for non-residential customers from October 1, 2002 until June 1, 2003; and

c) Delmarva shall prepare and file prior to November 1, 2002, a class cost of service study in sufficient detail to permit Delmarva or other parties to propose a resetting of distribution rates, with any such distribution rate change to become effective for non-residential customers no earlier than June 1, 2003, and on October 1, 2003 for residential customers.

7. In the event that the merger has not closed by June 30, 2002, but does close prior to October 1, 2002, then the foregoing provisions of subsection II.O.6., to the extent they are in conflict with any other provision(s) of this Settlement, shall be superseded by such other provision(s) of this Settlement. In the event that the merger has not closed by October 1, 2002, but is still pending, the Settling Parties agree to meet to discuss what, if any, modifications to this Settlement are appropriate.

8. With the exception of section II.F.5., II.H.3, and II.O.6 (incorporating by reference II.A.1, 2., and 3), the agreements, terms and conditions and provisions of this Settlement are contingent on the closing of the merger and, absent such closing, are of no force or effect.

III. *RESERVATIONS*

A. This Settlement represents a compromise for the purposes of settlement and shall not be regarded as a precedent with respect to any ratemaking or any other principle in any future case. No Settling Party necessarily agrees or disagrees with the treatment of any particular item, any procedure followed, or the resolution of any particular issue in agreeing to this Settlement other than as specified herein, except that the Settling Parties agree that the resolution of the issues herein, taken as a whole, results in just and reasonable rates, that the disposition of all other matters set forth in the Settlement are in the public convenience, necessity and interest and that, with the disposition of all such matters as set forth herein, the proposed merger indirectly affecting Delmarva and the acquisition of control of Delmarva and CCI by New RC, shall be in accordance with law, for a proper purpose, and consistent with the public interest, as those terms are used in 26 *Del. C.* § 215, and shall be in accordance with the provisions of 26 *Del. C.* § 1016.

B. The various provisions of the Settlement are not severable. None of the provisions shall become operative unless and until the Commission issues an order approving the Settlement as to all of the terms and conditions set forth herein without modifications or conditions. The Settlement shall be subject to waiver only by the unanimous written agreement of the Settling Parties. If any portion of this Settlement is modified, conditioned, or rejected by the Commission, the Settlement shall be considered null and void and each Settling Party individually reserves the right to proceed with the filing of testimony, briefs and evidentiary hearings as contemplated in the Commission's Orders in Docket No. 01-194. If the Settlement is rendered null and void by operation of this section III.B., the Settling Parties agree to enter into good faith negotiations to reach a new settlement. Once the Settlement has become operative under the terms of this section III.B., its terms may be revised or waived only by the unanimous written agreement of the Settling Parties.

IV. *CONCLUSION*

*17 IN WITNESS WHEREOF, intending to bind themselves and their successors and assigns, the undersigned parties have caused this Settlement to be signed by their duly-authorized representatives and the undersigned parties

further recommend and urge the Commission to issue an order expeditiously approving this Settlement and making the requesting findings and approvals set forth herein.

Randall V. Griffin	Connie S. McDowell
Delmarva Power & Light	Delaware Public Service
Company	Commission Staff
Kirk Emge	Kirk Emge
Potomac Electric Power Company	New R.C, Inc.
G. Arthur Padmore	David M. Kleppinger
Division of the Public Advocate	BOC Gases, Inc.
Louis R. Monacell,	Lance Haver
Delaware Electric Users Group	Consumers Education & Protective
	Association of Delaware
Michael A. Dennis	Eric M. Page
International Brotherhood of	Old Dominion Electric
Electrical Workers, Local 1307	Cooperative
Bernard J. August	E. Paul Bienvenue
Bernard J. August	Delaware Electric Cooperative

Attachment 1

P.S.C. Del. No. 8 — Electric

First Revised Leaf No. 38

Delmarva Power & Light Company d/b/a Conectiv Power Delivery

RULES AND REGULATIONS SECTION XIX — MARKET PRICED SUPPLY SERVICE ('MPSS')

Market Priced Supply Service ('MPSS') is the provision of electricity, ancillary, transmission and related services to Customers by the Company and is designed to recover the current market cost of electricity, ancillary and transmission services for combined Electric Supply & Delivery Service Customers. The Market Priced Supply Service charge includes the current market price for capacity, energy, ancillary services, and transmission service for the Company's service territory.

The Market Priced Supply Service is applicable to any customer who is served under Service Classifications: 'MGS-S', 'LGS-S', 'GS-P', 'GS-T', 'ORL', 'OL' or 'NCR', and who has purchased its electric supply services from an Electric Supplier, other than the Company, and returns to the Company for electric supply services for its account.

The Customer's account must remain on MPSS for at least one (1) billing month, after which, and beginning on the Customer's scheduled meter reading date, the account will be eligible to be served by an Electric Supplier. The Customer may not switch from the Company's Market Priced Supply Service to the Company's Standard Offer Service.

*18 The Market Priced Supply Service charge shall be a negotiated market price, if mutually agreeable to the Company and the Customer in each party's sole discretion, or the sum of the following billing components:

1. The market hourly energy charge which is determined by multiplying the Customer's hourly load, adjusted for the applicable loss adjustment factor for the Customer's service voltage level, with the hourly integrated DPL Zone Real Time Locational Marginal Priced ('LMP'), or its successor, as determined and reported by the PJM Interconnection, LLC ('PJM'). When a Customer's account does not have interval metering, the Customer's Service Classification's load profile data will be used to develop the hourly use by customer class that will be adjusted for losses. Using the hourly use and the hourly LMP, or its successor, a customer class average daily energy rate will be developed which will be applied to the Customer's Kwh usage for each day.

2. The annual ancillary charge which is determined by multiplying DPL's annual total ancillary service charges for the previous calendar year, as determined and reported by the PJM Interconnection, LLC ('PJM') and charged to the Company by the ratio of the Customer's annual peak load contribution for capacity obligation including losses, adjusted for the applicable PJM determined capacity reserve margin factor over Delmarva's annual capacity obligation including losses, adjusted for the applicable PJM determined capacity reserve margin factor. The annual ancillary charge will be divided by 12 and billed monthly. This ancillary charge supersedes and is in lieu of the 'Ancillary Service Energy Rate' component of the applicable Service Classification under which the Customer is receiving Delivery Service.

3. The capacity charge which is determined by multiplying the Customer's annual peak load contribution for capacity obligation including losses, adjusted for the applicable PJM determined capacity reserve margin factor, by DPL's average cost of capacity for the billing month. The average cost of capacity is the weighted average, based on 'Total MW Cleared,' and the Clearing Prices of the transactions reported in PJM Monthly and the Multi-Monthly Capacity Credit Markets that includes the billing month, adjusted for any PJM Daily Deficiency Penalties charged by PJM to DPL as a result of a shortfall between capacity acquired to serve MPSS customers and the capacity obligation including losses of such customers, as adjusted, excluding any such Penalties incurred as the result of Delmarva's waste, bad faith or abuse of discretion. MPSS customers shall not be charged any portion of a PJM Daily Deficiency Penalty charged by PJM to DPL as the result of a shortfall between capacity acquired to serve customers not served under the MPSS and the capacity obligations including losses, as adjusted, of such customers.

4. The transmission service charge which shall be as provided in the 'Transmission Rate' and/or the 'Transmission Demand Rate' components of the applicable Service Classification under which the Customer is receiving Delivery service.

*19 The market hourly energy prices and market daily capacity prices used for the Market Priced Supply Service are available on the PJM internet web site: *www.pjm.com.* In the event the Customer wishes to track or estimate its costs under this service, it is the Customer's responsibility to construct, operate and maintain, at its sole expense, all communications structures, equipment, and any other apparatus necessary to ensure its timely receipt of the market hourly energy prices and market daily capacity prices for the Customer's use in operating its facility.

Filed December xx, 2001 Effective with Meter Readings On and After October 1, 2002

Proposed Settlement in Docket No. 01-194

Attachment 2

Illustrative Examples of How Congestion Mechanism Works

1) No one else is ever obligated to contribute any funds toward relieving congestion.

2) But, the cost-effectiveness test looks initially only to the congestion costs of Delmarva and a portion of any net credits from congestion that Delmarva received during the congestion period. Thus, if Delmarva is the only entity paying to construct the upgrades, the project will be cost effective only if it permits Delmarva to avoid a sufficient amount of congestion to make the project economically viable.

3) Only congestion on the Delmarva peninsula 'counts.' That is for triggering purposes (1000 hours), only congestion hours for which one or more Delmarva facilities are listed as the Contingency on PJM's Off-Cost Operations data 'count,' subject to defined exclusions for forced generation and transmission outages and construction. For cost-effectiveness purposes, one looks at the total amount of congestion that would have been avoided if the analyzed facility(ies) had been in service. Special rules apply to adjust the cost-effectiveness test for periods in which there are FTR credits that exceed Delmarva's congestion charges and to earmark funds when cost-effective projects are identified but not constructed.

4) EXAMPLE 1:

STEP 1 ANALYSIS

In 2002, there are 1,200 hours of congestion on the Delmarva peninsula based on PJM's Off Cost Operations data.

Associated congestion costs for Delmarva is $200,000.

Associated congestion costs for ODEC is $100,000.

Associated congestion costs for other market participants is $50,000.

Analysis indicates that the least-cost option to reduce congestion levels below 1,000 is an upgrade to a Delmarva facility that would reduce congestion hours by 500 hours.

Analysis indicates that had the upgrade been in place during 2002, there would have been $100,000 less congestion for Delmarva, $80,000 less congestion for ODEC, and $20,000 less congestion for other market participants.

Congestion costs exceed FTR credits.

Estimated carrying cost of the facility is: $80,000.

Result: Project is cost-effective for Delmarva under the Step 1 Analysis to construct without a contribution from other entities. Estimated 'savings' for Delmarva are $100,000, and estimated carrying costs are $80,000. When transmission rates are next reset, rate base would increase by cost of project.

EXAMPLE 2:

*20 STEP 2 ANALYSIS

Same facts as above, except that:

Estimated carrying cost of the facility is $110,000, and During 2002, FTR credits on the PJM bills are $240,000 higher than Delmarva's congestion costs.

Step 1 Result: Project is not cost-effective for Delmarva to construct under the Step 1 Analysis. Estimated 'savings' for Delmarva are $100,000, but estimated carrying costs are $110,000.

Step 2 Result. The ratio of excess congestion over the total hours of congestion (200/1200) is multiplied against the $240,000 in net FTR credits, which result is deemed to provide an additional $20,000 in 'benefits' toward the cost-effectiveness test. Project is 'cost-effective' for Delmarva to construct. Estimated savings and deemed benefits are $100,000 plus $20,000 and estimated carrying costs are $110,000. When transmission rates are next reset, rate base would increase by the cost of the project minus the $20,000 in carry-forward net FTR credits applied.

EXAMPLE 3:

STEP 3 ANALYSIS

Same facts as in Example 2, except that Estimated carrying cost of the facility are $130,000; ODEC's load ratio share is 30%, and its congestion savings are calculated by ODEC to be $50,000.

STEP 1 Analysis Result: Project is not cost-effective for Delmarva to construct. Estimated 'savings' for Delmarva is $100,000, but estimated carrying costs are $130,000.

STEP 2 Analysis Result: Project is not cost-effective to construct. Estimated savings and deemed FTR benefits are $100,000 plus $20,000, but estimated carrying costs are $130,000.

STEP 3 Analysis Result. Other load serving entities are solicited for an additional contribution, plus CIAC tax effects. It is recognized that an entity making a load ratio share contribution plus CIAC tax effects would still be subject to a load-ratio share of any transmission rate increases caused by Delmarva's contribution to the project. In recognition of this, but without an intent to create a one-for-one offset, the contribution solicited would be no larger than necessary to close the 'gap.' That is, for example, ODEC would not be requested to provide 30% of the capital costs with annual carrying charges of $130,000 of project (plus CIAC tax effects), but rather only the capital costs associated with annual carrying charges of $10,000 (plus CIAC tax effects). Under this scenario, while Delmarva saves $100,000 in congestion costs and ODEC saves $50,000; Delmarva will expend capital associated with $120,000 in carrying costs, while ODEC will expend capital associated with $10,000. Presumably, ODEC would make a capital contribution in its own economic interest. When transmission rates are next reset, rate base would increase by the cost of the project minus the CIAC contributed by others and the $20,000 in carry-forward net FTR credits applied.

EXAMPLE 4

Same as in Example 3, but ODEC's calculation of its estimated congestion savings are only $5,000, and no other market participant makes a contribution.

*21 Result: Under all three Steps, the project is not cost-effective and is not constructed. Delmarva, however, carmarks $20,000 toward future projects and to the extent not offset in future years by a negative carry-forward net FTR credit, the rate base effect of such future projects would be reduced by $20,000.

Footnotes

1 We note that none of AES's exceptions challenge the merger among Delmarva, Conectiv, PEPCO, and New RC. Indeed, AES's counsel reiterated during her argument on AES's exceptions that AES was not taking issue with the merger itself. (Tr. at 368-69.)

2 CCI remains in existence as a telephone utility included in the Application notwithstanding a sale of most of its assets and its entire retail customer accounts to Cavalier Telephone, LLC under a separate transaction approved by this Commission.

3 The parties initial and reply briefs will be cited as 'IB' and 'RB,' respectively. I have not considered attachments to the briefs of certain parties that included non-record documents.

4 The section liberally is taken from the parties' briefs.

5 Mr. Rainey after filing his direct testimony left ODEC, and currently is employed as the Midwest regional market policy director for Texas Utilities. Tr. 332.

6 The Proposed Settlement is lengthy and complex, and this summary omits certain details not deemed significant.

7 The Commission's rules allow a party to undertake discovery at any time, and AES never sought any expedited response to any of its discovery on the Proposed Settlement.

8 The Commission should expect these customers to purchase the lowest cost electricity, and to take advantage of available regulatory choices to lower their costs, even if the result is higher costs to other customers.

9 It should be noted that CCI will technically remain in existence as a telephone utility and hence remains an applicant notwithstanding a sale of most of its assets and all of its retail customer accounts to Cavalier Telephone, LLC under a separate transaction.

10 For purposes of this Settlement, Separately Metered Space-Heating and Water Heating Services provided to customers whose primary meter is served under either the SGS-ND or the MGS-S classification will be treated as if served under SGS-ND. As discussed in greater detail in Docket No. 99-163, Delmarva's billing system does not provide separate identifiers that would permit a distinction to be made between these separately metered services provided to customers with primary meters served under SGS-ND and those served under MGS-S.

11 As used herein this subsection II.N., 'transmission construction' includes new construction of transmission lines and substations, and upgrades and rebuilds of existing facilities, but does not include maintenance. 'Transmission forced outages' means outages of transmission lines or substations that are from causes outside the control of Delmarva including but not limited to major storms, fires, and events of force majeure. It is understood that a major, unexpected, premature failure of equipment may trigger a study that would identify the least-cost, economic solution for congestion to be the replacement or upgrade of the equipment that failed.

12 'Incremental Avoided Congestion Charges' shall be computed as follows: use the hours of congestion avoided, multiplied by Delmarva's load in the DPL South Zone multiplied by the difference in LMP between DPL North and DPL South.

13 'Aggregate Congestion Costs' shall be defined as: Congestion charges incurred over the relevant period that are separately stated in the PJM congestion charge on Delmarva's PJM bills (including forward market purchases made through PJM e-schedules) plus congestion costs incurred for interchange transactions (and forward market purchases to the extent not made through PJM e-schedules) that are not reflected separately on the PJM bills. Congestion costs for interchange transactions will be calculated by multiplying the difference between the PJM Zone LMP and the DPL Zone LMP by the interchange transactions for each applicable hour.

End of Document

TAB 5

2012 WL 7149411 (Del.P.S.C.)
Slip Copy

Re Delmarva Power & Light Company

PSC Docket No. 11-528
Order No. 8265

Delaware Public Service Commission

December 18, 2012

APPEARANCES: On behalf of the Applicant Delmarva Power & Light Company: TODD L. GOODMAN, ESQ., Associate General Counsel, Pepco Holdings, Inc. On behalf of the Delaware Public Service Commission: JAMES McC. GEDDES, ESQ., Rate Counsel, JULIE M. DONOGHUE, ESQ., Deputy Attorney General, Delaware Department of Justice. On behalf of the Division of the Public Advocate: MICHAEL D. SHEEHY, Public Advocate, REGINA A. IORII, ESQ., Deputy Attorney General, Delaware Department of Justice. On behalf of the Delaware Energy Users Group ('DEUG '): MICHAEL J. QUINAN, ESQ., Christian & Barton, LLP. Intervenor, State Representative John Kowalko.

Before Winslow, chairman, and Conaway, Lester, Clark, commissioners.

BY THE COMMISSION:

ORDER NO. 8265

***AND NOW*, this 18th day of December, 2012:**

WHEREAS, the Delaware Public Service Commission (the 'Commission') has received and considered the Findings and Recommendations of the Hearing Examiner issued in the above-captioned docket, which was submitted after a duly-noticed public evidentiary hearing, and is attached hereto as Attachment 'A;' and

WHEREAS, the Hearing Examiner recommends that the Commission approve the Proposed Settlement Agreement (submitted into evidence as Hearing Exhibit No. 39 at the August 28, 2012 evidentiary hearing), and which is attached hereto as Attachment 'B;'; and

WHEREAS, State Representative Kowalko, an intervener in this Docket, filed written exceptions to the Hearing Examiner's Report taking issue with the amount of the settlement, as well as the right of Delmarva Power & Light Company ('Delmarva' or the 'Company') to recover the net book value associated with former analog meters that have been replaced by Delmarva as part of Delmarva's advanced metering infrastructure (also known as 'AMI'); and

WHEREAS, having heard and considered the arguments of the parties on the exceptions filed by the State Representative, the Commission finds that there exists a preponderance of evidence in the record developed by the Hearing Examiner supporting the proposed rates and tariff changes as just and reasonable, and that adoption of the Proposed Settlement Agreement is in the public interest;

NOW, THEREFORE, IT IS HEREBY ORDERED BY THE AFFIRMATIVE VOTE OF NOT FEWER THAN THREE COMMISSIONERS:

1. That by and in accordance with the affirmative vote of a majority of the Commissioners, the Commission hereby adopts the October 23, 2012 Findings and Recommendations of the Hearing Examiner recommending

approval of the Proposed Settlement Agreement and the proposed rates therein. (3-0, Chairman Winslow participating by telephone and not voting). The approved rates reflect an additional $22 million revenue requirement, or an approximate 0.4% decrease over the interim rates under bond that became effective July 3, 2012. The revenue requirement amount is based upon a capital structure of 49.61% equity and 50.3 9% long-term debt, an overall cost of capital of 7.38%, and a rate of return on common equity of 9.75%.

2. That the final approved rates will become effective with usage on or after the date of this Order.

3. That the Commission orders that new compliance tariff leaves be developed and filed with the Commission Staff for its review, which shall include the new electric distribution rates and which shall become effective with service on and after January 1, 2013.

4. Since the new approved rates are less than the existing distribution rates placed into effect on July 3, 2012, pursuant to 26 *Del. C.* § 306(a)(1), customers are entitled to a refund of overpayments since Delmarva's interim rate increase was placed into effect, with interest on the deferred amounts calculated in accordance with 26 *Del Admin. Code* §1003, which shall reflect Delmarva's short-term borrowing costs. Once final approved rates are in effect, the Company shall develop a rate refund plan for applying customer refunds. The Company shall then promptly file its plan with the Commission.

5. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

EXHIBIT 'A'

FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

October 23, 2012 Dr. Vincent Ikwuagwu Hearing Examiner

FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

I.

II. BACKGROUND

1. On December 2, 2011, Delmarva Power & Light Company ('Delmarva' or the 'Company') filed with the Delaware Public Service Commission (the 'Commission ') an Application to increase its electric distribution rates by $31,760,741, or 19.18% over present distribution rates, and for approval of other miscellaneous tariff modifications (the 'Application'). A typical residential customer using 1,000 kWh per month would experience an average monthly increase of $7.27 (from $144.48 to $151.75), or about a 5% increase in its total bill. Delmarva stated that the proposed rate increase primarily reflects its additional investment to improve reliability and safety, diversify its energy supply portfolio, expand and improve its customer service, and modernize its infrastructure. Delmarva further explained that it is making these investments in non-revenue producing plant at a time when revenue growth from customers is slowing, resulting in lower returns on invested capital. The Company sought an overall return of 7.87% (including a 10.75% return on equity) on an estimated rate base of $599,949,723. The Application was based on six months of actual data and six months of forecasted data through December 31, 2011.[1] (Ex. 2 at £ 3).

2. With its Application, Delmarva submitted direct testimony from Anthony J. Kamerick, Senior Vice President and Chief Financial Officer of Pepco Holdings, Inc. ('PHI'); Dr. Mark N. Lowry, President of Pacific Economics Group Research LLC; Julie M. Cannell, President of J.M. Cannell, Inc.; Robert B. Hevert, President of Concentric Energy Advisors, Inc.; Kevin M. McGowan, PHI's Vice President and Treasurer; Gary Stockbridge, President of PHI's Delmarva Region; W. Michael VonSteuben, Manager of Revenue Requirements and Regulatory Accounting for PHI's Regulatory Affairs Department; Jay C. Ziminsky, Manager, Revenue Requirements for

PHI'S Regulatory Affairs Department; Kathleen A. White, Assistant Controller; William M. Gausman, Senior Vice President for Strategic Initiatives at PHI; Charles R. Dickerson, PHI's Vice President for Customer Care; Elliott P. Tanos, PHI's Manager of Cost Allocation; and Marlene C. Santacecilia, a PHI Senior Regulatory Analyst.

3. In Order No. 8088 dated January 10, 2012, pursuant to 26 *Del. C.* §§306(a)(1) and 502 and 29 *Del. C.* ch. 101, the Commission initiated this docket, suspended the proposed full rate increase pending the completion of evidentiary hearings into the justness and reasonableness of the proposed rates and tariffs; designated Senior Hearing Examiner Ruth Ann Price to conduct such hearings and report to the Commission her proposed findings and recommendations concerning this matter; and allowed Delmarva to place into effect $2,500,000 of the proposed increase under bond on January 31, 2 012.

4. On February 17, 2012, pursuant to 29 Del. C. §8716, the Division of the Public Advocate (the 'Public Advocate') intervened in this proceeding to represent ratepayers' interests. The Delaware Energy Users Group ('DEUG'), the Delaware Department of Natural Resources and Environmental Control ('DNREC ') and State Representative John A. Kowalko filed motions to intervene, which were granted without objection.

5. After Senior Hearing Examiner Price resigned her position to become Deputy Public Advocate, the Commission, pursuant to 26 *Del. C.* §502 and 29 *Del. C.* ch. 101, appointed me to serve as the Hearing Examiner in Order No. 8114, dated February 23, 2012.

6. On March 2, 2012 Delmarva filed supplemental testimony from Messrs. McGowan, VonSteuben and Ziminsky, in which it updated its test period information to include twelve months of actual data through December 31, 2011 ('12+0 Update ') and updated (or increased) its suggested revenue shortfall to $33,186,072. (Exh. 16 at 2 and Sch. WMV S-1).

7. The Commission Staff ('Staff'), the Public Advocate and DEUG conducted extensive written discovery of the Company, and Staff and the Public Advocate performed a rate case audit of Delmarva's books and records extending over a period of several weeks.

8. In April 2012, the Commission conducted a public comment session on Delmarva's proposed rate increase in each of the three counties in which it provides electric distribution service. At each public comment session, Delmarva representatives summarized the Application and members of the public were afforded an opportunity to comment on the Application. At the New Castle County public comment session, one member of the public representing the Ad Hoc Committee of the Civic League of New Castle County opposed certain ratemaking changes that Delmarva was proposing. No members of the public attended the Kent County public comment session. At the Sussex County public session, a representative of the American Association of Retired Persons ('AARP') provided comments opposing the proposed increase. In addition, the Commission received over 1500 comments from customers opposing the Company's proposed rate increase, primarily by email from members of AARP.

9. On May 15, 2012, Staff filed direct testimony from David C. Parcell, President of Technical Associates, Inc.; Dr. Karl R. Pavlovic, Senior Consultant with Snavely King Majoros & O'Connor, Inc.; Matthew Hartigan, the Commission's Ombudsman; Gary B. Cohen, President of GBC Consulting, LLC; Michael J. McGarry, Sr., President and CEO of Blue Ridge Consulting Services; and David E. Peterson, Senior Consultant with Chesapeake Regulatory Consultants, Inc. The Public Advocate filed direct testimony from Andrea C. Crane, President of the Columbia Group, Inc.; James W. Daniel, Vice President of GDS Associates, Inc.; and Ralph C. Smith, Senior Regulatory Consultant with Larkin & Associates, PLLC. DEUG filed direct testimony from Nicholas Phillips, Jr., Managing Principal of Brubaker & Associates, Inc.

10. On June 19, 2012, pursuant to 26 *Del. C.* §302(b), Delmarva requested approval to implement an interim rate increase to increase its intrastate distribution revenues by an additional $22,224,360, under bond, subject to refund and under the same conditions as set forth in PSC Order No. 8088. The Commission approved this request in Order No. 8167 dated July 3, 2012, and Delmarva implemented this interim rate increase on July 3, 2012.

11. On June 21, 2012, the Company submitted rebuttal testimony from witnesses Kamerick, Lowry, Hevert,[2] McGowan, VonSteuben, Ziminsky, Gausman, Tanos, Cannell and Santacecilia.

12. On July 16, 2012, I conducted a prehearing teleconference with the participants, during which I requested a list of stipulated exhibits and uncontested issues, and directed that any pre-hearing motions be filed on or before July 25, 2012. On that date, Staff filed a motion to exclude Delmarva witness Cannell. I instructed Delmarva to file a response to Staff's motion by noon on July 26, 2012. On July 26, Delmarva submitted correspondence requesting additional time to review the authorities cited in and respond to Staff's motion. I conducted a teleconference on Delmarva's request, after which I granted Delmarva's request for additional time to respond.

13. On July 27, 2012, Staff counsel notified me via e-mail that Staff, Delmarva, the Public Advocate and DEUG had reached an agreement in principle to settle the case.

14. On July 30, 2012, I convened a duly-noticed evidentiary hearing. Counsel for Staff, the Public Advocate and Delmarva confirmed that they had reached an agreement in principle to settle the case and that they and DEUG were discussing a proposed settlement. After an off-the-record discussion, I directed the parties to finalize and file the proposed Settlement Agreement with the Commission no later than August 17, 2012. I further directed that an evidentiary hearing on the Settlement Agreement would be duly noticed for Tuesday, August 28, 2012.

15. On August 17, 2012, Staff's counsel submitted a Settlement Agreement executed by representatives of Staff, the Public Advocate, Delmarva and DEUG (the 'Settling Parties'). At the hearing on August 28, 2012, Staff's counsel presented a revised Settlement Agreement, including a statement that all pre-hearing motions were deemed withdrawn, but which otherwise did not substantively change the settlement agreement filed on August 17, 2012. (Ex. 39). The hearing participants stipulated to the admission of all of the prefiled testimony and the Settlement Agreement, although Rep. Kowalko observed that he was not agreeing that the Settlement Agreement should be approved. (Tr. 106). Delmarva, Staff and the Public Advocate each proffered a witness to testify regarding the Settlement Agreement and stand cross-examination.[3]

16. Upon the conclusion of the evidentiary hearing, I closed the record, consisting of 39 exhibits and 197 pages of transcript.

17. I have considered the entire record of this proceeding, and herein submit these Findings and Recommendations to the Commission for its consideration.

III. BRIEF SUMMARY OF THE PARTIES' POSITIONS

18. *Delmarva.* The Company selected a historical test year consisting of the twelve months ended June 30, 2011 and a partially projected test period consisting of the twelve months ending December 31, 2011. After making several adjustments to rate base and expenses, the Company calculated a revenue deficiency of $33,186,072, derived from an adjusted rate base of $572,556,602; an overall rate of return of 7.87% and cost of equity ('COE') of 10.75% on a capital structure consisting of 50.39% long-term debt and 49.61% common equity; and adjusted operating expenses of $141,613,107.

19. Delmarva also proposed several alternatives to traditional ratemaking practices designed to reduce what it called 'chronic' under earning due to regulatory lag (Ex. 3 at 12; Exh. 5 at 3): a surcharge to recover its investments in reliability plant in between rate cases (the 'Reliability Investment Mechanism' or 'RIM') (Ex. 3 at 13-14; Ex. 5 at 31-51); the option of a fully-forecasted test period (Ex. 5 at 27-30); revenue decoupling (*id.* at 17-23); and a multi-year rate plan. (*id.* at 20-27).

20. *Staff.* Staff did not contest the Company's test year or test period. Staff contended that Delmarva should be allowed a revenue requirement increase of $15,883,075, applied to an adjusted rate base of $533,839,479; an overall rate of return of 7.28% and COE of 9.55% on the Company's proposed capital structure; and adjusted operating income of $139,310,840. As will be discussed in further detail below, Staff opposed Delmarva's alternative regulation proposals and took issue with Delmarva's class cost of service study and proposed rate design.

21. *Public Advocate.* The Public Advocate also did not contest Delmarva's test year or test period. The Public Advocate calculated a revenue deficiency of $17,465,428 on an adjusted rate base of $561,924,297; an overall rate of return of 6.69% and COE of 8.73% on a proposed capital structure consisting of 49.05% long-term debt, 2.67% short-term debt, and 48.29% common equity; and adjusted operating income of $27,364,689. The Public Advocate also opposed Delmarva's alternative ratemaking proposals and challenged certain aspects of Delmarva's cost of service study and requested rate design.

22. *DEUG.* DEUG challenged certain aspects of Delmarva's class cost of service study and rate design. It sponsored adjustments to Delmarva's cost of service study and proposed changes to Delmarva's rate design.

IV. SUMMARY OF THE PREFILED TESTIMONY

A. Delmarva's Direct Testimony.

23. Delmarva witness Kamerick provided an overview of the Application. (Ex. 3 at 3). He testified that Delmarva was spending millions of dollars to replace infrastructure to enhance the reliability of its distribution system and provide for future customer usage growth, but it did not have the opportunity to earn its authorized return on equity because revenue growth was not keeping pace with increased rate base and operating costs. (*Id.* at 8-11). According to Mr. Kamerick, traditional ratemaking practices when the Company is investing in non-revenue producing plant, and at a time when revenue growth from customers is slowing, results in rates that are outdated as soon as they are approved, and thus are insufficient to provide Delmarva with the opportunity to earn its authorized return given the pace of growth in its rate base and capital expenses. (*Id.* at 12-13). He urged the Commission to consider implementing some or all of four proposed regulatory lag mitigation mechanisms to counter the effects of regulatory lag. Mr Kamerick contended that failure to address the negative effects of regulatory lag could result in more frequent (perhaps annual) rate cases and higher capital costs, all of which are detrimental to Delmarva and its customers. (*Id.* at 16-21).

24. Company witness Lowry addressed several proposed alternative regulatory mechanisms. He testified that regulatory lag was a serious threat to Delmarva's ability to earn its authorized return on equity, especially given its planned capital expenditures over the next few years. After describing and discussing various alternative regulatory mechanisms to address regulatory lag, he recommended that the Commission approve the RIM for reliability-related capital expenditures and permit Delmarva the option to use a fully-forecasted test year in future rate cases. Dr. Lowry also suggested that the Commission could consider a form of a multi-year rate plan in combination with the RIM. (*Id.* at 4, 50-52).

25. Company witness Cannell testified about investors' perspective regarding Delmarva, including their perception of its risk as a result of its capital expenditures and current macroeconomic conditions, their expectations for a constructive regulatory environment, and their expectations for its return on equity. (Ex. 7 at 3-45).

26. Company witness Hevert testified regarding the Company's COE. He calculated the Company's COE at 10.75%, using constant growth Discounted Cash Flow ('DCF '), Capital Asset Pricing Model ('CAPM'), and Bond Yield Plus Risk Premium ('RP ') models applied to a group of nine proxy electric companies. (Ex. 9 at 4, 25-26). Additionally, he considered Delmarva's comparatively small size, its regulatory environment, its proposed capital expenditure plans, whether revenue decoupling (if approved) would have a measurable effect on its COE, and costs associated with common stock issuances, although he testified that he did not make any explicit adjustments to his calculated COE for these factors. (*Id.* at 4, 47-69).

27. Company witness McGowan presented Delmarva's capital structure and current credit ratings. (Ex. 11 at 3). He testified that the Company's proposed capital structure, consisting of 49.48% common equity and 50.52% long-term debt, was consistent with industry practice and averages, and was reasonable in light of the mean capital structures of the proxy groups used to determine Delmarva's COE. (*Id.* at 4-5). He explained how he calculated the Company's proposed 5.05% cost of long-term debt. (*Id.* at 3, 9). He described why Delmarva's investment-grade credit ratings [4] were important and how customers would benefit from those investment-grade credit ratings. (*Id.* at 6-8). Finally, he testified regarding how Delmarva calculated the projected revenue requirement for the first year of the rate-effective period and described the key assumptions underlying those projections. (*Id.* at 9-10).

28. Company witness Stockbridge testified regarding Delmarva's role in the community, including how its core values of safety, accountability, integrity, diversity and excellence shape its corporate policies. (Ex. 14 at 4-7). He described the Company's primary focus on providing safe and reliable service at the lowest possible cost to customers, and how all customer and community relationships flow from this principle. He described how Delmarva and its employees support community non-profit and volunteer organizations whose goals are improving quality of life in the community and providing educational opportunities. (*Id.* at 7-8). He explained the Company's leading role in the electric industry and in improving the environment, such as its involvement in initiatives for increasing energy efficiency, reducing C02 emissions, maintaining the indigenous plant and animal life along its rights-of-way, purchasing significant amounts of on-shore wind and solar power, and implementing advanced metering infrastructure ('AMI') technology. (*Id.* at 9-13).

29. Company witness VonSteuben presented the selection of Delmarva's test year and test period, the development of Delmarva's distribution-related revenue requirement request, and the per-book earnings and rate base used in the Application. He sponsored certain minimum filing requirements ('MFRs') and adjustments to rate base and earnings, and summarized adjustments that Delmarva was proposing. He also discussed the Company's inability to earn its authorized return on equity. (Ex. 15 at 2-27).

30. Company witness Ziminsky presented certain adjustments used to develop Delmarva's proposed revenue requirement. (Ex. 18 at 2-12). He described the components of the $3 9 million balance of the AMI regulatory asset: (1) $25.8 million for analog meters retired early due to AMI deployment; [5] (2) $11.1 million of deferred operations and maintenance ('O&M') expense incurred from August 2009 through the end of the test period; [6] (3) $3.1 million of returns representing recovery of and on the AMI regulatory asset and net incremental AMI rate base, calculated at the Company's authorized rate of return; (4) $600,000 of incremental depreciation expense for AMI meters compared to the replaced analog meters; [7] and (5) a $1.6 million offset to the AMI regulatory asset related to O&M expense savings from: (a) reduced manual meter reading costs; (b) remote connect/disconnect functionality; (c) reduced off-cycle meter reading labor costs; (d) improved billing activities; (e) asset optimization; (f) elimination of hardware, software and O&M costs for the Itron handheld data collection system; (g) reduced expenses related to revenue protection; (h) improved complaint call handling; and (i) reduced volume of customer calls related to metering. (*Id.* at 15-17). The Company's revenue requirement also included $72 million of AMI-related plant. (*Id.* at 15).

31. Mr. Ziminsky testified that Delmarva proposed to implement recovery of the AMI regulatory asset over time (without the need for a full base rate proceeding) based on its successful completion of certain milestones. Initially, Delmarva proposed to phase-in 50% of the AMI regulatory asset balance in December 2012 upon successful implementation of the remote connect/disconnect functionality and Phase 1 of its dynamic pricing program. (*Id.* at 17-18). Delmarva would phase-in the remaining balance of the AMI regulatory asset in December 2013 upon successfully implementing Phase 2 of dynamic pricing and launching enrollment for its proposed direct load control program. All costs would be amortized over 15 years, with rate base treatment for the unamortized balance. (*Id.* at 17-19).

32. Company witness White supported the actual amounts recorded in Delmarva's books and records for the test period and sponsored certain MFRs. (Ex. 21 at 2-3). She testified about Delmarva's cost accounting

structure and observed that several independent audits of its cost accounting manual had concluded that affiliate allocations and charges were consistent with the cost accounting manual and the service agreement. (*Id.* at 4-7).

33. Company witness Gausman testified regarding Delmarva's plans and budgets for non-AMI-related plant replacements and improvements to enhance system reliability and accommodate increased load. (Ex. 22 at 4-8). Next, he described the AMI system and projected schedule for completion. (*Id.* at 8-17). He specifically observed that during Hurricane Irene, the AMI system allowed Delmarva to verify outage status, thus avoiding customer call-backs and/or truck rolls to affected areas and reducing outage length. (*Id.* at 11). Last, he described the proposed RIM, including how Delmarva envisioned it would operate in practice and the benefits Delmarva believed it would provide to both its customers and the Company. (*Id.* at 17-25).

34. Company witness Dickerson discussed Delmarva's initiatives to improve customer service, including additional personnel, infrastructure, storm or emergency-related responses, and customer education and research. (Ex. 24 at 1-7).

35. Company witness Tanos presented Delmarva's class cost of service study. He described the key processes involved in cost allocation, the Company's cost of service model and its cost allocation method. (Ex. 25 at 4-14).

36. Company witness Santacecelia testified about the rate design supporting the Delmarva's proposed rate increase. She also sponsored certain MFRs and tariff modifications (including the language for the proposed RIM), updated the rate design that was being addressed in the modified fixed variable ('MFV') revenue decoupling docket in a separate working group, and provided an update on the status of the Utility Facility Relocation Charge. (Ex. 27 at 2-13).

B. Delmarva's Supplemental Testimony

37. Company witness McGowan updated Delmarva's proposed capital structure to reflect its actual capital structure as of December 31, 2011 (50.39% long-term debt and 49.61% common equity), and reduced the embedded cost of long-term debt from 5.05% to 5.04%. (Ex. 12 at 1-2).

38. Company witness VonSteuben updated Delmarva's financial and accounting data based on actual results for the twelve months ending December 31, 2011. The updated data indicated a revenue requirement deficiency of $33,186,072. (Ex. 16 at 1-4).

39. Company witness Ziminsky updated the adjustments and the AMI regulatory asset discussed in his direct testimony. As updated, through the twelve months ended December 31, 2011, the $38.8 million AMI regulatory asset balance consisted of: (1) $25.5 million of analog meters retired early due to AMI deployment; (2) $10.9 million of deferred O&M expense incurred from August 2 00 9 through the end of the test period; (3) $3.6 million of returns representing recovery of and on the total AMI regulatory asset and net incremental AMI rate base, calculated at the Company's authorized rate of return; (4) $700,000 of incremental depreciation expense for AMI meters compared to the replaced analog meters; and (5) a $1.9 million offset to the AMI regulatory asset related to O&M expense savings. (Ex. 19 at 2-3).

C. Staff

40. Staff witness Cohen addressed the Company's AMI proposals. He contended that many of the benefits asociated with the AMI technology that Delmarva had filed in its 2007 Blueprint for the Future Business Case had not yet been realized, and that recovery of the AMI regulatory asset should be deferred until those benefits had been realized over a substantial period of time and Staff had reviewed and audited them. (Ex. 33 at 3-18). Importantly for purposes of these Recommendations, Mr. Cohen attached to his testimony a copy of the 2007 Business Case, in which Delmarva stated the following about accumulated depreciation on legacy analog meters:

As stated in PHI's February 6, 2 007 Blueprint for the Future filing and in the 2007 NARUC Resolution to Remove Barriers to the Broad Implementation of Advanced Metering Infrastructure, the deployment of AMI technology will require the removal and disposition of existing meters that are not fully depreciated and the replacement of, or significant

modification to, existing meter reading, communications, and customer billing and information infrastructure. To encourage the implementation of this new technology the Commission should adopt ratemaking policies that remove a utility's disincentive toward demand-side resources that reduce throughput; provide for timely cost recovery of prudently incurred AMI expenditures, *including accelerated recovery of investment in existing metering infrastructure*, in order to provide cash flow to help finance new AMI deployment; and provide depreciation lives for ami that take into account the speed and nature of change in metering technology. The business case reflects depreciation lives for AMI that take into the [sic] account the speed and nature of the change in metering technology. The business case reflects a recovery period of fifteen years for the AMI investment and five years for recovery of the remaining costs associated with the existing metering system. As of December 31, 2006, Delmarva's existing electric metering system had a remaining net book value of about $26 million ... .

Ex. 33 at Sch. GC-2, pp. 30-31) (emphasis added).

41. Staff witness Hartigan addressed the Company's customer service initiatives. He recommended effecting a monitoring plan to ensure that the additional expense being incurred by Delmarva actually improves the customer experience. He recommended disallowing the new CIS costs because they were not yet used and useful. Finally, he noted that Staff had received 1,500 written public comments unanimously opposing the proposed rate increase. He characterized the comments as demonstrating a high level of distrust and animosity toward the Company and pointing out that the timing of the rate increase was difficult because of the hardships endured by Delmarva's customers due to the economic recession. (Ex. 34 at 2-8).

42. Staff witness McGarry examined PHI's intercompany allocations after the changes in its corporate structure resulting from its sale of Conectiv Energy. He concluded that the Service Company services provided and charged to Delmarva aligned reasonably-well with the governing documents; there was no reason to question the reasonableness or accuracy of the Service Company costs charged to Delmarva; the Company's verification of service and allocation agreement compliance demonstrated compliance and appropriate monitoring; and the Conectiv Energy divestiture did not negatively affect Delmarva's ratepayers. (Ex. 35 at 2-8).

43. Staff witness Parcell testified regarding the Company's COE. He accepted Delmarva's proposed capital structure and cost of long-term debt. (Ex. 36 at 2-3, 5-7). He calculated the Company's COE within a range of 9.35-9.75% (with a 9.55% midpoint), using constant growth DCF, CAPM, and Comparable Earnings models applied to two groups of proxy companies (the same group that Mr. Hevert used and another group comprised of ten publicly-traded electric companies). (*Id.* at 2-3, 5, 14-25). Mr. Parcell disagreed with certain aspects of Mr. Hevert's application of his cost of capital methodologies, contending that Mr. Hevert's model inputs, as well as the methodologies themselves, were systematically biased to inflate his COE conclusions. (*Id.* at 30-34). He also disputed Ms. Cannell's testimony that the increased risk of investing in electric companies justified a higher COE than Delmarva's currently-authorized one. (*Id.* at 34-35). Finally, Mr. Parcell testified that Delmarva's risk would be reduced significantly if the Commission approved any of Delmarva's proposed alternative regulatory mechanisms, and that reduced risk should be reflected in a lower COE. (*Id.* at 26-28).

44. Staff witness Pavlovic addressed Delmarva's proposed alternative regulatory mechanisms, its class cost of service study, and its proposed rate design. He concluded that the proposed RIM was unnecessary because Delmarva had not established that it suffered from chronic attrition or regulatory lag; furthermore, the proposed RIM lacked sufficient detail for evaluation and was flawed in numerous respects. (Ex. 3 7 at 5, 28). Next, he expressed concern with Delmarva's class cost of service study and concluded that it should not be used either to distribute the requested revenue requirement among the customer classes or to establish the classes' customer charges. (*Id.* at 5-6, 28-37). Last, he found that Delmarva's proposed rate design inappropriately included volumetric rate components, but recommended accepting it pending final design, adoption and implementation of the MFV rate design. (*Id.* at 6, 34-38).

45. Staff witness Peterson addressed Delmarva's rate base and operating income issues. He challenged several of Delmarva's proposed rate base adjustments, including certain reliability plant adjustments and inclusion

of Construction Work in Progress ('CWIP'), among others. Regarding operating expenses, Mr. Peterson made a number of proposed adjustments, the effect of which reduced the Company's claimed expense levels for the test period and increased its earnings, thereby reducing its proposed revenue deficiency. (Ex. 38 at 3-34).

D. Public Advocate.

46. Public Advocate witness Crane testified regarding the Company's COE. First, she recommended a capital structure consisting of 48.29% common equity, 2.67% short-term debt (at a cost of $47,000) and 49.05% long-term debt. (Ex. 29 at 8-12). She accepted the Company's proposed cost of long-term debt. (*Id.* at 13). Using constant growth DCF and CAPM models applied to the same proxy companies that Company witness Hevert used, and giving 75% weight to her DCF result and 25% weight to her CAPM result, she derived an 8.73% COE for Delmarva. (Id. at 5, 16-27). In this regard, she noted that all of the proxy companies owned generation assets, which made them significantly more risky than Delmarva. (*Id.* at 16-17). Ms. Crane denied that a higher COE than Delmarva's currently-authorized one was justified, and discussed how capital costs had decreased since the Company's last base rate case, Docket No. 09-414. (*Id.* at 29-32). Ms. Crane also disagreed with certain aspects of Mr. Hevert's application of his cost of capital methodologies. (*Id.* at 18-27). Last, Ms. Crane testified that Delmarva's risk would be reduced significantly if the Commission approved any of Delmarva's proposed alternative regulatory mechanisms, and that reduced risk should be reflected in a lower COE. (*Id.* at 33-36).

47. Public Advocate witness Smith addressed Delmarva's rate base and operating income issues. He challenged several of Delmarva's proposed rate base and operating expense adjustments and recommended several other adjustments to Delmarva's rate base and operating expense. (Ex. 31 at 2-3, 7-37). He opposed the Company's proposed RIM (*id.* at 37-42), and expressed concerns similar to Staff witness Cohen's regarding the Company's proposed phase-in of the ami regulatory asset. (*Id.* at 43-46).

48. Public Advocate witness Daniel addressed Delmarva's proposed alternative regulatory mechanisms, its class cost of service study, and its proposed rate design. He first contended that the proposed RIM was unnecessary because Delmarva had not established that it suffered from chronic attrition or regulatory lag. He further argued that the proposed RIM lacked sufficient detail for evaluation and was flawed in many respects. (Ex. 31 at 8-19). He rejected Delmarva's other alternative regulatory mechanisms as unnecessary and unsupported. (*Id.* at 19-22). Next, Mr. Daniel identified several issues with Delmarva's class cost of service study, and concluded that unless Delmarva re-ran its COSS with 2011 load data, the Commission should apply the approved system average increase to all classes whose revenues had been identified as not recovering costs. (*Id.* at 22-30). He further recommended replacing the labor allocation factor Delmarva used to allocate the costs of its general and common plant accounts (FERC Accounts 389-399) with the total distribution plant allocation factor to more accurately reflect the principle of cost causation. (*Id.* at 31-32). Mr. Daniel next testified that Delmarva's proposed customer charge design conflicted with the price signal associated with energy conservation, and was significantly higher than most utilities near its service area. (*Id.* at 32-43). Last, Mr. Daniel opposed the MPV revenue-decoupled rate design, noting that revenue decoupling would reduce Delmarva's risk but the Company had not reduced its requested return on equity to reflect this reduced risk. (*Id.* at 42-49).

E. DEUG

49. DEUG witness Phillips addressed the Company's class cost of service study and rate design. He testified that Delmarva had incorrectly classified certain distribution-related costs, which caused the rates paid by General Service Secondary and General Service Primary customers to be greater than the cost of serving them. He recommended that the class cost of service study be modified to classify a portion of those costs to the customer function. (Ex. 32 at 3, 10-19). He further testified that the class cost of service study appeared to overallocate distribution plant investment to the General Service Transmission class, and so that class should not receive any rate increase. (*Id.* at 3, 19-21). Finally, he recommended that the Commission not implement the MFV rate design. (*Id.* at 3, 24-25).

F. Delmarva's Rebuttal Testimony

50. Company witness Kamerick submitted testimony rebutting Staff's and the Public Advocate's contentions regarding regulatory lag and their opposition to Delmarva's proposed alternative regulatory mechanisms. He also addressed the effect that Staff's and the Public Advocate's proposed revenue requirements and COE would have on Delmarva as it attempted to obtain capital while its reliability capital expenditures were ongoing. (Ex. 4 at 3-19). Last, he took issue with certain of Staff's and the Public Advocate's expense adjustments. (*Id.* at 19-28).

51. Company witness Lowry also provided rebuttal to Staff's and the Public Advocate's positions on the proposed RIM and other alternative regulatory mechanisms. (Ex. 6 at 28).

52. Company witness Cannell addressed Staff's and the Public Advocate's proposed COEs. She testified that their recommendations did not meet investors' expectations and would harm customers because of their negative impact on investor perceptions regarding PHI's earnings, dividend prospects and quality and consistency of regulation. (Ex. 8 at 1-9).

53. Company witness Hevert also provided rebuttal to Staff's and the Public Advocate's proposed COEs. He updated his COE models to reflect data through May 12, 2012, and also performed a multi-stage DCF analysis for his proxy group. He testified that the updated data continued to support his original COE recommendation of 10.75%. (Ex. 10 at 2-78).

54. Company witness McGowan addressed Staff's and the Public Advocate's proposed treatment of Delmarva's credit facilities costs and the Public Advocate's recommended inclusion of short-term debt in the capital structure. (Ex. 13 at 1-7).

55. Company witness VonSteuben listed certain uncontested issues, identified Staff and Public Advocate adjustments or positions that the Company had accepted, and addressed other rate base and operating expense adjustments that Staff and the Public Advocate either had challenged or had made themselves. (Ex. 17 at 2-30).

56. Company witness Ziminsky listed additional uncontested issues and addressed other rate base and operating expense adjustments that Staff and the Public Advocate either had challenged or had made themselves. (Ex. 20 at 2-32). He also discussed the Company's proposal for the AMI phase-in and contested Staff's and the Public Advocate's positions regarding the proposed phase-in. (*Id.* at 33-37).

57. Company witness Gausman submitted rebuttal regarding Staff's and the Public Advocate's opposition to the proposed RIM and their positions that the Company had not yet realized substantial AMI-related benefits. (Ex. 23 at 2-25).

58. Company witness Tanos responded to the class cost of service study issues that Staff, the Public Advocate and DEUG raised. (Ex. 2 6 at 1-9).

59. Company witness Santacecelia addressed Staff's, the Public Advocate's and DEUG's criticisms of Delmarva's proposed rate design, including an update to the MFV. (Ex. 28 at 1-9).

V. THE PROPOSED SETTLEMENT

60. As mentioned previously, the Settling Parties advised me on July 27, 2012, the last business day before the scheduled evidentiary hearings, that they had reached a settlement in principle. On July 30, 2012, the first day of the scheduled evidentiary hearings, the Settling Parties stated on the record that they had reached a settlement in principle and asked for additional time to draft a proposed written settlement agreement. I instructed the Settling Parties to submit the proposed settlement agreement on or before August 17, and rescheduled the evidentiary hearing for August 28, 2012.

61. Counsel for Staff submitted a fully-executed settlement agreement on August 17, 2012, as instructed, and a revised agreement on August 28, 2012 containing minor changes and language regarding the

resolution of all pending motions. The Settling Parties executed this revised settlement agreement during the August 28 evidentiary hearing and I admitted it into the record as Exhibit 3 9 (the 'Settlement'). [8]

62. The salient provisions of the Settlement are as follows. First, the total revenue requirement increase will be $22 million, which represents an approximate 13.3% increase over the rates approved in Docket No. 09-414. Compared to the Docket No. 09-414 rates, a typical residential customer using 1,000 kWh per month will experience a 3.28% increase in its total bill, from $136.86 per month to $141.35 per month. Because the current interim rates were designed to collect more than $22 million, Delmarva will credit (or refund to former customers) the approximately $227,030 per month excess revenue collected from July 3, 2012 (the effective date of the second interim rate increase) through the date the Commission approves the Settlement. As a result of the credit/refund, the typical residential customer's total bill will actually decrease by 0.4%, from $141.93 per month to $141.3 5 per month. The credit/refund shall be made proportionally to all customers whose rates increased on July 3, 2012 and who became customers thereafter using the same billing determinants used for the interim rate increase. (Ex. 39 at ¶¶ 11-12).

63. No other modification to the Cost of Service issues raised in this case will be made at this time. (*Id.* at ¶ 12).

64. The Company's capital structure will consist of 49.61% equity and 50.39% long-term debt, an overall cost of capital of 7.38%, and its authorized rate of return on common equity will be 9.75%. (*Id.* at ¶ 13).

65. The Settlement also resolves litigation among Delmarva, Staff and the Public Advocate regarding cost recovery related to a tax-related ratemaking error in Docket No. 04-391, Standard Offer Service (SOS) Supply, for the SOS years beginning June 1, 2012, 2013 and 2014 (the 'SOS Docket'). In that docket, Delmarva alleged that it paid various taxes assessed by taxing authorities upon its SOS customers but failed to collect the amounts of those taxes in its SOS customers' bills. Thus, pursuant to Section IX E of its Delaware Electric Tariff, Delmarva sought recovery over three years of $6,346,205 for the amounts it paid on behalf of SOS customers but failed to collect (the 'SOS Under Recovery'). $2,115,401.67 of that amount is currently being collected in SOS customers' rates, subject to refund. The Settling Parties resolved the SOS Under Recovery issue as follows:

a. The SOS Under recovery is reduced to $3,346,205 ('$3.4 million') and will no longer be subject to refund. Delmarva will collect the $3.4 million from its SOS customers over three SOS years beginning June 1, 2012, without carrying costs.

b. In conjunction with the commencement of the AMI Asset Phase-In (discussed *infra*) and the adjustment of distribution base rates to reflect the $22 million Settlement revenue requirement, SOS rates will be adjusted on January 1, 2013 to reflect a collection of $1,115,401.67 for the 2012-2013 SOS year. There will be a true-up each year. The total amount collected will not exceed $3,346,205. $1,115,401.67 will be collected in the 2013-14 SOS year, and the remaining $1,115,401.67 will be collected in the 2014-15 SOS year.

(Ex. 39 at ¶¶ 14-15)

66. As discussed previously, in Order No. 7420 (Docket No. 07-28), the Commission authorized Delmarva to establish a regulatory asset for operating costs associated with AMI deployment. In Order No. 8011 (Docket No. 09-414), the Commission reiterated its decision to authorize an AMI regulatory asset in Order No. 742 0 and approved recovery of $1.47 million of deferred incremental AMI expenses, amortized over 15 years with the unamortized balance included in rate base. As of December 31, 2011, the balance of that regulatory asset was $38.8 million. (Ex. 19 at 3). The Settling Parties propose to recover the AMI regulatory asset in rates as follows: (1) 20% on January 1, 2013; (2) 50% of the balance of the AMI regulatory asset on June 1, 2013; and (3) the remaining balance on June 1, 2014. However, the Settlement provides that with respect to the June 2013 and June 2014 phase-in dates, Delmarva will be permitted to include in rates only such amounts related to AMI capability

that has been reasonably functioning as planned and has been enabled for at least 95% of customers eligible for the respective capability for at least sixty (60) days prior to the applicable June phase-in date. Thus, for example:

• If by June 1, 2013 Delmarva has not been remotely connecting and disconnecting *at least* 95% of its eligible customers who request that service for a period *of at least* 60 days, then it may not include in rates the value of that portion of the AMI regulatory asset in June 2013.

• If Delmarva has not demonstrated success in Phase 1 of its dynamic pricing program for residential field acceptance test customers *at least* 60 days prior to June 1, 2013, then it may not include in rates the value of that portion of the AMI regulatory asset in June 2013.

• If by June 1, 2014, Delmarva has not implemented remote connect/disconnect capability for failure to pay and other involuntary service terminations (theft of services, safety violations, etc.) for a period of *at least* 60 days, then it may not include in rates the value of that portion of the AMI regulatory asset in June 2014.

• If by June 1, 2014, Delmarva has not demonstrated success in Phase 2 of its dynamic pricing program for its residential customer base *at least* 60 days prior to June 1, 2013, then it may not include in rates the value of that portion of the AMI regulatory asset in June 2014.

Delmarva must file its request to include the June 2013 and June 2014 portions of the AMI regulatory asset balance at least 75 days before each applicable date, and in no case later than March 15 of each year. (Ex. 39 at £ 16, n.3 and Attachment 1).

67. Additionally, the Settlement assigns a percentage value to each AMI capability identified in Attachment 1 that Delmarva expects to implement during each June phase-in rate adjustment. The Settlement provides that if a capability scheduled to go into effect by the particular June phase-in rate adjustment date has either not been enabled for at least 95% of the eligible customers or has not met the 60 day functionality period, *then*: (a) the amount placed into rates during that June phase-in rate adjustment will be reduced by the percentage value associated with that capability; (b) that same amount will remain in the AMI Asset and will not be eligible to be placed into rates until the following June 1; and (c) the annual $1,115,401.67 SOS recovery will be reduced as follows: (a) a total of $250,000 will be at risk for failure to meet capabilities: (i) $125,000 will be at risk for the SOS year beginning June 1, 2013; and (ii) $125,000 will be at risk for the SOS year beginning June 1, 2014. If a capability scheduled to go into effect by the particular June phase-in rate adjustment date has either not been enabled for at least 95% of the eligible customers or has not been reasonably functioning as planned for at least 60 days prior to the applicable June 1 date, then the percentage value associated with that capability will be applied to the $125,000 at risk on the relevant June 1 phase-in date and that percentage of the $125,000 will be deducted from that same year's SOS rates. (Ex. 39 at £ 16 and Attachment 1). Furthermore, any such deductions from the $250,000 at risk for failure to meet capabilities will be permanent, meaning that Delmarva will not be allowed to collect such amounts from customers at any time in the future.

68. The Settling Parties will meet and discuss several other issues outside this rate proceeding in the hope of resolving each of them: (1) establishing metric(s) for the reporting and/or approval of reliability projects going forward so that customers are aware of how investment in Delmarva's plant in service benefits them in a quantifiable manner; (2) alternative regulatory methodologies that would include, but not be limited to, multi-year rate plans; and (3) improving the Company's compliance with the financial reporting requirements under the Delaware Administrative Code. (Ex. 39 at £ 17).

69. The Settlement provides that Delmarva will continue to hold quarterly AMI meetings, during which it will update Staff and the Public Advocate on the continued diffusion of AMI technology into its system, until either further order of this Commission or such time as Staff, the Public Advocate and

Delmarva agree that the AMI system is substantially developed and operational to the extent that such regular meetings are no longer necessary. Furthermore, Staff and the Public Advocate will continue to share with Delmarva their recommendations, ideas and/or concerns relating to AMI. (Ex. 39 at £ 19).

70. The $22 million distribution rate increase will be implemented on an across-the-board basis, such that the percentage change in the distribution revenues will be the same for all of Delmarva's Service Classifications, except that the GS-T customer class shall receive no increase in distribution rates.

71. The Settling Parties are not asking the Commission to approve ratemaking treatment for any issues not specifically addressed in the Settlement. The parties are free to raise those issues in a future base rate or other regulatory proceeding. The purpose of the Settlement is to provide just and reasonable rates for Delmarva's customers, which the Settling Parties believe the terms of the Settlement accomplish. In addition, because the Settlement was a product of extensive negotiation, the Settling Parties have conditioned the Settlement on the Commission approving it in its entirety without any modification. (Ex. 39 at £ 21).

VI. THE AUGUST 28, 2012 EVIDENTIARY HEARING

72. On August 28, 2012, I conducted the duly-noticed evidentiary hearing on the Settlement. Thomas Noyes attended the hearing on behalf of DNREC. In response to my question regarding DNREC's position on the Settlement, Mr. Noyes stated that DNREC had intervened in the docket in the event that revenue decoupling was addressed, and since the Settlement was silent on that issue, DNREC did not oppose the Settlement. (Tr. at 105-06). State Representative and Intervenor John Kowalko also attended the evidentiary hearing and opposed the Settlement. His opposition will be discussed below.

73. The Settling Parties each presented a witness to testify regarding the Settlement.[9] Each witness was subject to questioning from me and from the parties and interveners who participated in the hearing.

74. Delmarva witness Ziminsky testified that the Settlement resulted in just and reasonable rates and was in the public interest. He noted that the Settling Parties represented different stakeholder groups with diverse interests. He stated that the Settlement struck a balance between the Company's need for additional revenue to enable it to provide safe and reliable service and maintain its financial health and the difficult economic position that Delmarva recognized many of its customers faced, and that the Settlement enabled the Company to recover the cost of providing safe and reliable service to its customers. He testified that Delmarva had increased its reliability plant in service by more than $125 million since its last base rate case. (Tr. at 111-12). He further described the process by which the Settling Parties had reached their agreement, noting that the participants had investigated the claimed amount of the AMI regulatory asset, and that Staff had conducted a field audit at which it examined the items comprising the AMI regulatory asset and their costs. (*Id.* at 154).

75. With respect to AMI, Mr. Ziminsky testified that AMI deployment had saved over $2.3 million in meter reading costs, which were then offset against the AMI regulatory asset, and which the Company's customers would continue to realize annually. (*Id.* at 114-16). He described the business case for AMI deployment discussed in the Company's 2007 Blueprint for the Future, and testified that the Company and the Commission had concluded that the benefits of AMI outweighed the costs. (*Id.* at 117-18). He identified two categories of savings that customers would realize from AMI: (a) operational savings, which the Company estimated to be $6.44 million annually, and (b) supply-side savings, which on a 15-year net present value basis ranged from $36 million to $107 million based on the level of customer participation in dynamic pricing and other energy efficiency initiatives. (*Id.* at 118-19, 130-31). He provided examples of the benefits of AMI deployment, such as the Company's ability to 'ping' meters during storms to determine the status of service at a particular address; he noted that during Hurricane Irene this allowed the Company to avoid sending 582 trucks and related personnel to particular addresses or areas, and resulted in faster service restoration when outages did occur. (*Id.* at 134-36). Mr. Ziminsky testified that the regulatory asset is being amortized over

15 years, and the effect of the phase-in on the typical residential consumer's total bill is approximately $1.53 per month once the entire regulatory asset was phased into rates. (*Id.* at 120-28, 160-61). He also observed that if the Company did not achieve the functionalities identified in the Settlement at the time it sought recovery, it would not be permitted to place the portion of the regulatory asset associated with those functionalities into rates until the following year. In addition, he explained that a non-recoverable financial penalty to Delmarva in the form of bill credits would result from any failure by Delmarva to achieve AMI functionalities in a timely manner. He further noted that Staff and the Public Advocate would review the Company's filing to determine that those functionalities were in fact being realized before Delmarva could recover that portion of the AMI regulatory asset. (*Id.* at 125-28, 133-34, 163-64). Finally, he testified that Delmarva, Staff and the Public Advocate had negotiated the method of and conditions on the recovery of the AMI regulatory asset over the course of two and one-half weeks. (*Id.* at 159-60).

76. Rep. Kowalko cross-examined Mr. Ziminsky regarding the Settlement's provisions for recovery of the AMI regulatory asset. Rep. Kowalko questioned why there would be any rate increase associated with the AMI asset recovery since the proposed amortization resulted in an annual $5 million revenue requirement but customers would allegedly experience $6.4 million in annual savings. (Tr. at 138). Mr. Ziminsky explained that much of these savings was in the form of avoided costs — costs of service that Delmarva would no longer be incurring with AMI in place and therefore would no longer be collected from customers in rates. (*Id.* at 139-40). Rep. Kowalko asked about the composition of the AMI regulatory asset, and specifically focused on whether it included costs associated with the early retirement of the analog meters. (*Id.* at 140-44, 148). Finally, he questioned Mr. Ziminsky about the amount of the AMI regulatory asset, and again specifically focused on the amount of the asset related to early retirement of the analog meters. (*Id.* at 153-54).

77. Staff witness Patricia A. Gannon, who was Staff's case manager for this docket, also testified that the Settlement balanced the interests of the parties in the case, and therefore resulted in just and reasonable rates and was in the public interest. (*Id.* at 174). She testified that she was involved in the extensive discussions regarding settlement of the AMI regulatory asset issue, and that the resolution of that issue as set forth in the Settlement was different from what the Company had proposed. (*Id.*). She stated that the Settlement's treatment of the collection of the undepreciated balance of the analog meters was consistent with prior Commission decisions and regulatory policy in general, and that if utilities were precluded from recovering accelerated depreciation on early-retired plant, they would have no incentive to embrace new technology. (*Id.* at 175). Last, she stated that the AMI technology would aid the Company in its efforts to maintain and improve reliability. (*Id.* at 176).

78. Rep. Kowalko questioned Ms. Gannon regarding the cost of the analog meters being retired. Ms. Gannon responded that the parties were aware of the original cost of the meters being retired and testified that their average life was thirty years. (*Id.* at 177-78). Upon being asked why she thought the Settlement was reasonable even though the revenue requirement amount was higher than Staff's filed position, Ms. Gannon replied that it reflected a compromise of the parties' various positions based on what each party believed it would achieve through further litigation. (*Id.* at 178).

79. Finally, Public Advocate Michael D. Sheehy, who was also involved in the settlement negotiations, testified that the Settlement resulted in just and reasonable rates and was in the public interest. First, he addressed what he believed to be some confusion in the comparison of the AMI regulatory asset and expenses. He explained that the regulatory asset represented capital investment made 'up front' to reduce expenses over time (hence the net present value). The recovery of the AMI regulatory asset simply replaces the expense recovery stream with a capital recovery stream. (*Id.* at 180). Next, he noted when money is spent on an asset; the utility is entitled to a return both of and on that asset. The return *of* the money spent on the asset is depreciation; the rate of return is the return *on* the money spent on the asset. (*Id.* at 180-81).

80. Mr. Sheehy then discussed why he believed the Settlement resulted in just and reasonable rates and was in the public interest. First, he examines whether there is sufficient evidence presented to allow evaluation of the parties' positions. He answered that question affirmatively. (*Id.* at 181). Second, he evaluates a settlement in terms of whether the Commission is likely to reach a different result. In this case, he concluded that the $22 million agreed revenue requirement fell within the ranges of what was probable based on his assessment of what the Commission was likely to decide on each of the contested issues. (*Id.* at 181-82). Third, he considers whether the Settlement makes sense. In

this case, he concluded that it did; he noted that the Public Advocate's office had supported AMI diffusion in Delaware and believes that such diffusion was critical to Delaware's future economic development. (*Id.* at 182). He further noted that the Settlement reduced the cost of the rate case that would otherwise be recovered in rates. Last, he testified that he was guided by the Public Utilities Act, which instructs the Commission to encourage the resolution of cases by stipulations and settlement, and noted that he favors initiatives that reduce the cost of regulation. (*Id.* at 182-83).

81. Rep. Kowalko asked Mr. Sheehy whether it was in the public interest to consider so many issues in the context of one case. Mr. Sheehy responded that it was important to examine revenue, expenses and capital items together in order to ascertain their relationship to each other and what rates should be. He testified that single-issue ratemaking is 'a bad idea.' (*Id.* at 184-85).

VII. DISCUSSION

82. The Commission has jurisdiction over this matter. *26 Del. C.* § 201(a).

83. The Settling Parties, representing diverse interests, have testified that the Settlement results in just and reasonable rates and is in the public interest. The Settlement was reached after significant discovery and negotiations by the Settling Parties. I find their testimony in support of the Settlement persuasive. For the reasons that follow, I recommend that the Commission approve the Settlement notwithstanding Rep. Kowalko's opposition. [10]

84. First, as Public Advocate Sheehy observed, 26 *Del. C.* §512(a) provides that '[i]nsofar as practicable, the Commission shall encourage the resolution of matters brought before it through stipulations and settlements.' Clearly, this reflects a legislative intent that the Commission welcome settlements of part or all of a case, as long as the settlement results in just and reasonable rates and is in the public interest.

85. Second, the fact that the Settling Parties represent diverse interests is persuasive to me. Delmarva's interest must focus upon achieving rates that allow it to recover its costs of providing service and an opportunity to earn a fair rate of return. Staff is required to balance the utility's and ratepayers' interests. 29 *Del. C.* §8716(d)(2) charges the Public Advocate with advocating the lowest reasonable rates for consumers consistent with maintaining adequate utility service and an equitable distribution of rates among all the utility's customer classes. [11] DEUG represents a number of large industrial customers of Delmarva. Despite these distinct interests and responsibilities, these parties have reached an agreement. This, in my view, is a substantial factor weighing in favor of approving the Settlement [12]

86. There is substantial evidence on the record in this case to support my recommendation that the Settlement be approved. 29 *Del. C.* § 10142(d). [13] First, it is clear that every participant that submitted prefiled testimony (Delmarva, Staff and the Public Advocate) recommended some increase in the revenue requirement, but it is also clear that the Settlement was the product of extensive negotiation and compromise. The record evidence supported a revenue requirement increase of anywhere between $15,883,075 (Staff's recommendation, assuming the Commission decided every contested monetary issue in Staff's favor) to $33,186,072 (Delmarva's requested revenue requirement, assuming the Commission decided every contested monetary issue in Delmarva's favor). I find that the Commission in all likelihood would not likely have decided every contested issue in favor of any one of the participants that submitted prefiled testimony; rather, it would more likely have balanced each parties position against certain regulatory principles and reached some compromise between the various positions taken by the parties. In this context, I note that the Settlement's revenue requirement increase is substantially less than the Company's updated request of $33,186,072.

87. Additionally, it should be remembered that the Company proposed several alternative regulatory treatments designed to streamline its recovery of reliability plant expenditures and to give it a reasonable opportunity to earn its authorized return on equity — the RIM surcharge, a fully-forecasted test period, revenue decoupling, and a multi-year rate plan. As discussed previously, Staff and the Public Advocate opposed these alternative regulatory treatments on several grounds. Specifically addressing the RIM, Staff and the Public Advocate

argued that the Company's proposal increased the regulatory burden on them and the Commission. I note without passing judgment on the RIM's merits that as proposed, it envisioned an additional regulatory proceeding. It cannot be assumed, however, that the Commission would not have been persuaded by Delmarva's contentions and policy arguments. The fact that none of these alternative regulatory treatments are included in the Settlement is a significant concession by Delmarva, even if that concession cannot be reduced to dollars and cents.

88. Third, the Settlement also resolves the SOS Under Recovery issue from the SOS Docket. In that regard, the Settlement confers a clear benefit on Delmarva's SOS customers because Delmarva agreed to forego recovery of one-half of the amount of SOS Under Recovery to which it claimed it was entitled. Reasonable minds might differ as to how much the Company was entitled to recover, but it seems apparent that it would have been entitled to recover some of the SOS Under Recovery under the Commission-approved tariff language.

89. Next, I find that Rep. Kowalko's objection to including in the AMI regulatory asset the unrecovered cost of the early-retired analog meters and the cost of the new AMI meters should be rejected for several reasons. First, I note that the Company raised the issue in its Business Case filed in Docket No. 07-28, which was filed in August 2 007, over five years ago. Docket No. 07-28 was an open, public docket. The Business Case was available to anyone who wished to examine it. As previously discussed, Delmarva specifically identified the undepreciated cost of the legacy meters as a component of a regulatory asset should the Commission choose that route rather than some other recovery mechanism such as a surcharge. (Ex. 33 at Sch. GS-2 pp. 30-31).

90. Second, when the Commission authorized Delmarva to establish a regulatory asset for costs associated with the deployment of AMI, it was aware that the Company was seeking recovery of the undepreciated cost of the legacy meters and the costs of the new AMI meters. *See* Order No. 7420 dated Sept. 16, 2008 at 3. And just over a year ago, the Commission reaffirmed its approval for the creation of a regulatory asset in Order No. 8111 in Docket No. 09-414 (Aug. 9, 2011). *See id.* at £ 221.

91. Third, Rep. Kowalko did not proffer any evidence to support his argument that the undepreciated balance of the legacy meter costs or the cost of the AMI meters should not be included in the AMI regulatory asset. As my counsel noted at the evidentiary hearing, Rep. Kowalko was granted intervenor status in January 2012. He had copies of all prefiled testimony; he had notice of the procedural schedule; he received copies of all discovery and all non-confidential discovery responses; and he had an opportunity to submit testimony setting forth his opposition to including the undepreciated balance of the legacy meter cost and the cost of the new AMI meters in rates. (Tr. at 149-50). The prefiled testimony made clear that Delmarva was requesting recovery of the undepreciated balance of the legacy meters and the new AMI meters. (Ex. 18 at 15-16). Notwithstanding Delmarva's testimony, I am aware of no evidence presented during the course of this case that indicated any disagreement with rate recovery of the legacy meter cost and the cost of the new AMI meters in the AMI regulatory asset. Rather, the only issue raised in the proceeding regarding the collection of these costs was the timing of their collection. Any claim of surprise that these items would be recovered in rates as part of the AMI regulatory asset, and included as part of the Settlement, does not have support in this record.

92. The Company clearly described the AMI-related regulatory assets in its direct testimony:

Q: *Please describe the AMI-related regulatory assets.*

A: The descriptions of the AMI-related regulatory assets as well as balances as of October 2011 were:

• *The net book value of non-AMI meters which have been retired early due to AMI deployment. The balance is currently $25.8 million.*

* * *

• AMI Returns representing *recovery of* an on the appropriate costs associated with the AMI regulatory assets as well as AMI incremental net rate base (*AMI meters net of non-AMI meters*, communication equipment, software and hardware).

... .

• *Incremental depreciation expense of AMI meters' expense compared to the expense related to the replaced meters.* Customer's [sic] current base rates reflect the inclusion of the depreciation expense level associated with the retired meters. As AMI meters have replaced the non-AMI meters, the Company has recorded a higher level of depreciation expense for financial reporting purposes compared to the depreciation expense established in rates. Since customers have been paying for a lower level of meter depreciation expense than the Company has recorded for financial reporting purposes, the incremental depreciation expense has been recorded in a regulatory asset. The balance is currently $0.6 million.

(Ex. 18 at 15-16) (emphasis added).

93. Fourth, I find that the substance of Rep. Kowalko's objection lacks merit. As Staff witness Gannon testified, depreciation on utility plant is a normal utility cost. I also agree with her observation that utilities would not embrace new technology if they could not recover the costs of that new technology. I am satisfied that the phased-in recovery schedule of the AMI regulatory asset proposed in the Settlement (which I note is not the same schedule that the Company sought) properly matches the benefits of the new technology with the timing of the cost recovery. I also note that the Company risks significant delay in recovery of the AMI regulatory asset and financial penalties if it does not meet the Settlement's functionality deadlines and conditions. Moreover, if the Company is penalized, the amount of the penalty will be given to its customers through bill credits. I believe that the phased-in cost recovery, along with the fact that the Company is subject to financial risk for failure to meet functionality deadlines and conditions, protects Delmarva ratepayers.

94. Finally, other state commissions addressing the appropriate treatment of costs associated with a conversion to smart meters have included the undepreciated balance of the legacy meter cost and the cost of the new AMI meters in customers' rates. *See, e.g.*, In the Matter of Application of South Kentucky Rural Electric Cooperative for an Adjustment of Electric Rates, 2012 Ky. PUC LEXIS 222, *37 (Ky. PUC March 30, 2012) ('The Commission's use of the 15-year amortization period will ensure that the entire cost of the AMI project, which includes the loss on mechanical meters, will be recognized over the AMI project's estimated useful life of 15 years'); *Application of Nevada Power Company dlbla NV Energy for Approval of its 2010-2029 Triennial Integrated Resource Plan*, 2010 Nev. PUC LEXIS 71, *137 (Nev. PUC July 30, 2010) (creating 'a regulatory asset for the stranded non-AMI electric meter costs').

The Settlement's proposed treatment will provide the Company with the opportunity to recover its investment costs and earn a return on the non-AMI meters currently in rates. Moreover, the AMI-related savings that will accrue as AMI is used for more purposes will be offset against the regulatory asset balance, and the proposed implementation of recovery provides the Company with incentives to achieve those operational savings, which will benefit customers through reduced rates.

95. Finally, I am aware that there has been a claim that the Delaware Electric Cooperative ('DEC') did not charge its customers for its conversion to AMI. First, I have seen no evidence that DEC has implemented AMI or any advanced metering system comparable to that which Delmarva is implementing. Second, to the extent that it is claimed that DEC or any other electric cooperative 'did not charge its customers' for an AMI conversion, that claim is not entirely true. Both companies provide electric distribution service, but the similarity ends there. DEC is a cooperative, which means that its customers own it. It is a nonprofit organization, which means that whatever profits are left at the end of a date certain, after all expenses have been paid and investments made, are returned to the members. It is deregulated, which means that it can charge its customers whatever amount it sees fit. Although DEC customers did not directly pay the costs associated with AMI deployment in their service territory, they did pay indirectly through reimbursements that were reduced by the amount of DEC's investment in AMI. Delmarva is not a non-profit organization; its customers do not own

Delmarva and do not receive reimbursements at the end of a certain time period. Thus, to compare DEC to Delmarva with respect to deployment of advanced metering, or any other utility equipment, is akin to comparing apples to oranges.

VIII. RECOMMENDATIONS.

96. In summary, and for the reasons stated above, I find that the proposed Settlement results in just and reasonable rates and is in the public interest. Overall, it represents a fair resolution of the issues raised in this case. A proposed Order implementing the foregoing recommendations is attached hereto as Exhibit 'B' for the Commission's consideration.

97. Accordingly, I recommend that the Commission adopt this Report and approve the Settlement Agreement, confirming that the settlement rates can be placed into effect as of the date of the Commission Order approving the Settlement. Such approved rates and tariff revisions shall remain effective until changed by further Commission Order. Respectfully submitted, ___ Dr. Vincent O. Ikwuagwu Hearing Examiner Dated: October 23, 2012

EXHIBIT 'B'

delmarva power A PHI Company

November 2, 2012

VIA EMAIL AND HAND DELIVERY Ms. Alisa Bentley Secretary Delaware Public Service Commission 861 Silver Lake Boulevard Dover, DE 19904

Re: PSC Docket No. 11-528 — Delmarva Power Electric Base Rate Case *Compliance Filing for Rates Effective January 1, 2013*

Dear Ms. Bentley:

Attached please find the compliance filing of Delmarva Power & Light Company ('Delmarva') in Docket No. 11-528 for purposes of implementing rate changes that will occur on January 1, 2013, should the Commission approve the Recommendations of Hearing Examiner Ikwuagwu issued on October 23, 2012. The Commission's consideration of the Hearing Examiner's Report is scheduled for November 29, 2012.

Normally, Delmarva does not make compliance filings prior to the Commission's decision regarding a hearing examiner's recommendation. In the instant case, however, where the proposed settlement involves issues from multiple dockets, Delmarva believes it is preferable to make this filing sufficiently in advance of the January 1, 2013 effective date to provide Commission Staff and DPA with sufficient opportunity to carefully review the issues. Of course, should the Commission modify or reject the Hearing Examiner's Recommendations (in whole or in part) on November 29, 2012, Delmarva will amend this compliance filing accordingly.

In support of this compliance filing, we have included several attachments. This filing is designed to implement the following changes to base rates on January 1, 2013 as a result of the Proposed Settlement in this docket. Attached are:

• Attachment A: consists of the rate design workpapers to implement the $22,000,000 rate increase as agreed to in the Settlement Agreement in Section II paragraph 11

• Attachment B: consists of the workpapers that identify the revenue requirement associated with 20% of the AMI Asset to be put into rates effective January 1, 2013 as agreed to in the Settlement Agreement in Section II paragraph 16 ($1,198,935)

• Attachment C: consists of the rate design workpapers to implement the $1,198,935 revenue requirement associated with the first phase-in of the AMI Regulatory Asset. This rate design is inclusive of the $22,000,000 provided for in Section II paragraph 11, and provides for an increase in distribution revenues of $23,198,935

• Attachment D: consists of the compliance tariffs which implement the total revenue requirement $23,198,935 to be effective January 1, 2013

• Attachment E: consists of billing comparisons that detail the impacts of the January 1, 2013 rates. Because interim rates of $24,834,360 were put into effect on July 3, 2012 per Commission Order No. 8167, the rates that will go into effect on January 1, 2013 will result in a decrease for the typical residential customer

The $22,000,000 revenue increase referenced in Section II paragraph 11 of the Settlement Agreement provides Delmarva with less annual revenues than the interim rate increase implemented on July 3, 2012. Therefore, customers will receive a credit refund as referenced in Section II paragraph 12 of the Settlement Agreement. As in prior base rate cases, once a final order in the case is received, Delmarva will develop and present a refund plan which will include the specific details related to the refunds.

The Proposed Settlement also includes the resolution of an issue in another docket — Docket No. 04-391, which is the annual filing for standard offer service (the 'SOS Docket'). Because the resolution of that issue relates to another docket, we will make a companion compliance filing in the SOS Docket under separate cover.

As always, should you have any questions or need further information, please feel free to contact either me or Heather Hall (302-454-4828) at your convenience. Respectfully, Signature Todd L. Goodman cc: Service List in Docket No. 11-528

Attachment A

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MONTHLY CHARGES AND RATES

SERVICE CLASSIFICATION

OUTDOOR LIGHTING 'OL' — OPTIONAL EQUIPMENT MONTHLY RATE

For service provided under the 'Company Owned Equipment' Service Category, the Additional Monthly charge listed below shall be applicable, in addition to the above applicable OL Monthly Charges, for the respective non-standard optional equipment requested by and used to serve the Customer:

.Pp

• Additional Monthly Charge	
1. Ornamental, Decorative or Floodlighting Luminaires	$3.22
(This amount to be added to Service Category 'A')	
2. Poles	
A. Wood 25 ft. to 40 ft.	$5.78
B. Fiberglass or Aluminum, less than 25 ft.	$5.79
C. Fiberglass 25 ft. to 40 ft.	$10.28
D. Aluminum, Non-Breakaway, 25 ft. to 40 ft.	$15.43
E. Aluminum, Breakaway, 30 ft. to 45 ft.	$19.84

F. Metal Pole 25 ft. to 40 ft.	$5.77
(Included in Service Category B)	
(Not available after January 1, 1984)	
G. Stainless Steel Pole 25 ft. to 40 ft.	$15.43
(Not available after June 1, 1984)	
(This amount to be added to Service Category 'A')	
3. Turn of Century Luminaire, including pole.	
(This amount to be added to Service Category 'A')	
(Enclosed Luminaire with Bracket)	
A. Style A	$16.77
B. Style V	$11.57

Attachment E

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Footnotes

1 The evidentiary hearing exhibits will be cited herein as 'Ex. ___.' References to the pages of the Evidentiary Hearing Transcript will be cited as 'T-___.' Schedules from the Company's Application or pre-filed testimony will be referred to as 'Sch. ___.'

2 Between Delmarva's direct and rebuttal testimony, Mr. Hevert became managing partner of Sussex Economic Advisors, LLC. Ex. 10 at 1.

3 DEUG's counsel asked to be excused from the evidentiary hearing in light of its participation in the proposed settlement. By e-mail dated August 27, 2012, I granted DEUG's request provided that it arrange for its prefiled testimony to be entered into the record, which was done.

4 Delmarva's long-term corporate unsecured debt is rated BBB+ by standard & Poor's, Baa2 by Moody's, and A- by Pitch. (Ex. 11 at 5).

5 This is the net book value of the early-retired analog meters. (Ex. 18 at 15).

6 The Commission approved recovery of the deferred O&M costs incurred before August 2009 in Delmarva's last base rate case, Docket No. 09-414. (Ex. 18 at 15).

7 Mr. Ziminsky explained that as analog meters have been replaced with AMI meters, the Company has recorded a higher level of depreciation expense for the analog meters for financial reporting purposes. Since customers have been paying a lower

level of meter depreciation expense than Delmarva has recorded for financial reporting purposes, Delmarva recorded the incremental depreciation expense in the AMI regulatory asset. (Ex. 18 at 16).

8 The revised Settlement includes the provision withdrawing all pre-hearing motions. (Ex. 39 at £ 20).

9 As noted previously, although DEUG was a party to the Settlement, I granted its counsel's request not to be present at the evidentiary hearing. The Public Advocate supplied a copy of DEUG's prefiled testimony for the record.

10 Section 512(c) of the Public Utilities Act provides that the Commission may approve settlements that are not supported by all parties if it finds that the settlement is in the public interest. 26 *Del. C.* §512(c).

11 In this regard, I note that Rep. Kowalko stated at the evidentiary hearing that he was representing the ratepayers' interests. (Tr. at 147). I do not address the merits of that assertion, but simply note that the enabling legislation for the Public Advocate places that duty on him.

12 I observe that the Delaware Superior Court has placed significant weight on the Public Advocate's support of a settlement as being in the public interest since that entity is charged with protecting Delaware's ratepayers. *Constellation NewEnergy, Inc. v. Public Service Commission*, Del. Super., 825 A.2d 872, 883 (2003).

13 'Substantial evidence is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. It must be more than a scintilla, but may be less than a preponderance of the evidence.' Olney v. Cooch, Del. Supr., 325 A.2d 610, 614 (1981); *Price v. State of Delaware Board of Trustees*, Del. Super., 2010 Del. Super. LEXIS 120, *5, Young, J. (Mar. 22, 2010).

End of Document

TAB 6

2000 WL 1035896 (Del.P.S.C.), 202 P.U.R.4th 53

Re Delmarva Power and Light Company dba Conectiv Power Delivery

PSC Docket No. 99-582
Order No. 5469

Delaware Public Service Commission

June 20, 2000

Before Twilley, vice chairman and McRae, Puglisi and McClelland, Commissioners.

BY THE COMMISSION:

AND NOW, this 20th day of June, A.D. 2000;

WHEREAS, the Commission has received and considered the findings and recommendations of the Hearing Examiner dated May 5, 2000 in the above-captioned docket, which was submitted after a duly noticed public evidentiary hearing; and

WHEREAS, the Hearing Examiner recommends that the proposed settlement, as executed by representatives of Delmarva Power & Light Company, the Commission Staff, and the Division of Public Advocate, be adopted without modification; and

WHEREAS, the Hearing Examiner finds that the proposed settlement is in the public interest and, accordingly, recommends approval of the proposed Code of Conduct attached to the settlement; recommends that the Commission not adopt a GENCO Code of Conduct; and recommends that the Commission approve the proposed Cost Accounting Manual as modified pursuant to the settlement; and

WHEREAS, the Commission having determined, based upon the record developed below, including the findings and recommendations of the Hearing Examiner, and such investigation and inquiry as each Commissioner deems appropriate, that the proposed settlement, dated May 5, 2000, including the Code of Conduct attached thereto, should be approved without modification and be allowed to go into effect; and

WHEREAS, the Commission further determines that the approvals granted herein are 'without prejudice,' thus permitting any party, or other interested party, to later ask the Commission to revisit, and change, any portions of the Settlement, the Code of Conduct, or the Cost Accounting Manual; now, therefore,

IT IS ORDERED:

1. That by and in accordance with the affirmative vote of the majority of the Commissioners, the Commission hereby adopts the May 5, 2000 findings and recommendations of the Hearing Examiner, appended to the original hereof as Exhibit 'A.'

2. That the proposed settlement is adopted as a reasonable resolution of this proceeding and its terms and conditions incorporated therein.

3. That, in adopting the Hearing Examiner's findings and recommendations, the Commission does so 'without prejudice,' and, thus, expressly reserves to the parties, and other interested persons, the opportunity to request the Commission to revisit portions of the Settlement, the Code of Conduct, or the Cost Accounting Manual approved by this Order.

4. That the Commission reserves the jurisdiction and authority to enter such further Orders in this matter as may be deemed necessary or proper.

EXHIBIT 'A'

FINDINGS AND RECOMMENDATIONS OF THE HEARING EXAMINER

G. Arthur Padmore, duly appointed Hearing Examiner in this Docket pursuant to 26 *Del. C.* § 502 and 29 *Del. C.* Ch. 101, by Commission Order No. 5293, dated December 1, 1999, reports to the Commission as follows:

I. *APPEARANCES*

On behalf of the Applicant, Delmarva Power & Light Company: CHRISTIE DAY LEISER, ESQUIRE, Delmarva Power & Light Company, POTTER ANDERSON & COROON LLP, BY: GREGORY A. INSKIP, ESQUIRE, On behalf of the Intervenors (in alphabetical order): Cable Television Association of MD, DE & DC: WAYNE O'DELL, President, Delaware Energy Users Group: CHRISTIAN & BARTON, L.L.P., BY: LOUIS R. MONACELL, ESQUIRE, CLIONA M. ROBB, ESQUIRE, The Division of the Public Advocate ('DPA '): PATRICIA A. STOWELL, The Public Advocate, Enron Capital and Trade Resources, Inc., WOLF, BLOCK, SCHORR AND SOLIS-COHEN LLP, BY: GERALD GORNISH, ESQUIRE, Mid-Atlantic Power Supply Association, ALEXANDER & CLEAVER, BY: O. RAY BOURLAND, III, ESQUIRE, THOMAS W. KINNANE, ESQUIRE, Shell Energy Service Company, LLC, ALEXANDER & CLEAVER, BY: O. RAY BOURLAND, III, ESQUIRE, THOMAS W. KINNANE, ESQUIRE, On behalf of the Public Service Commission Staff ('Staff '): ASHBY & GEDDES, BY: JAMES McC. GEDDES, ESQUIRE, REGINA A. IORII, ESQUIRE, II. *BACKGROUND*

In March 1999, the Delaware General Assembly enacted the 'Electric Utility Restructuring Act of 1999' 72 Del. Laws c. 10 (March 31, 1999) ('the Act'). The Act substantially overhauled how electric supply service would be supplied in this State. By PSC Order No. 5206 (Aug. 31, 1999), the Commission approved a restructuring plan for Delmarva Power & Light Company, d/b/a Conectiv Power Delivery ('the Company,' 'Conectiv,' or 'Delmarva') under the Act. As part of such approval, the Commission directed that Delmarva's present Code of Conduct should remain in place but that a new docket should be opened to consider what changes to that Code might be necessary to address the deregulation of electric supply services under the Act. The Commission also directed that such a docket must be completed no later than June 30, 2000. (PSC Order No. 5218 at ¶ 5.)

At the time that it issued Order No. 5206, the Commission was also reviewing a proposed modification to Delmarva's Cost Accounting Manual ('CAM ') in Docket No. 98-424. In light of the conclusions reached in Order No. 5206, the Commission determined that it would be more efficient to review any changes to the then controlling CAM in conjunction with the Commission decision to similarly revisit the Company's present Code of Conduct in light of the Act. Thus, the Commission suspended all further proceedings in PSC Docket No. 98-424 and directed Delmarva to file, on or before November 15, 1999, a new proposed Cost Accounting Manual and new proposed Code of Conduct to govern activities and interplay between the regulated and unregulated divisions, affiliates, subsidiaries, and Delmarva's parent.

In drafting the new proposed CAM and Code of Conduct, the Commission directed that the Company consider: (a) the determinations made by the Commission in PSC Findings, Opinion, and Order No. 4706; (b) the requirements imposed by the Act; (c) the positions of the parties in PSC Docket No. 99-163; and (d) the audit reports to be filed under PSC Orders Nos. 4706 and 4768. (*Id.* at ¶ 7.)

On November 15, 1999, the Company filed an application seeking approval of a Code of Conduct and a CAM. Included in that filing was the written testimony of: J. Mack Wathen, Director of Finance and Regulatory Affairs for Conectiv;

James P. Lavin, Controller for Conectiv; and Dr. Alfred E. Kahn, the Robert Julius Thorne Professor of Political Economy, Emeritus, Cornell University and Special Consultant with National Economic Research Associates, Inc.

As directed by the Commission in Order No. 5218, Delmarva provided copies of the filing to the Division of the Public Advocate ('DPA'), each entity or person appearing on the Service List in PSC Docket No. 97-65, and each entity appearing on the Service List in PSC Docket No. 99-163.

By Order No. 5293, dated December 1, 1999, the Commission opened this docket and assigned the matter to this Hearing Examiner for further proceedings. Order No. 5293 also directed that the Company publish notice of its filing and that such notice should include information on how to intervene in this proceeding. The Company complied. (Ex. 1.) The Delaware Energy Users Group ('DEUG'), the Cable Telecommunications Association of Maryland, Delaware & DC, the Mid-Atlantic Power Supply Association ('MAPSA'), Shell Energy Services Company, LLC ('Shell'), and Enron Capital and Trade Resources, Inc. ('Enron '), petitioned for, and were granted, leave to intervene in this docket.

The public notice also informed interested persons who had not previously intervened of the opportunity to file comments on or before February 28, 2000. No person did.

On March 6, 2000, Staff filed the direct testimony of witnesses Robert L. Stright of Liberty Consulting and Rajnish Barua, the Commission's Regulatory Policy Administrator. On the same date, the DPA filed the direct testimony of its witness, Andrea C. Crane of The Columbia Group, Inc. On March 29, 2000, the Company filed the rebuttal testimony of Messrs. Wathen and Lavin, and Dr. Kahn. No other party filed testimony or otherwise participated in this proceeding.

On April 4, 2000, one day before public hearings concerning the proposed Code of Conduct and CAM were scheduled to begin, Counsel for Delmarva presented the Hearing Examiner with a proposed settlement of this docket that had been executed by the Company, the DPA, and the Staff. Attached to the proposed settlement was a revised Code of Conduct.

The duly publicized evidentiary hearing which was scheduled to be conducted on April 5, 2000 was held in order to review the proposed Code of Conduct and the proposals set forth in the settlement agreement.

Witnesses for the Company (Messrs. Wathen and Lavin), Staff (Mr. Stright and Dr. Barua), and the DPA (Ms. Crane) testified at the hearing. Dr. Kahn's pre-filed direct and rebuttal testimony was also offered and admitted into evidence without objection. Other than the settling parties, no other person appeared at or participated in the hearing.

The settlement and the thereto attached revised Code were admitted into evidence (Ex. 4) and are attached hereto as Attachment 'A.'

On the same date, the Hearing Examiner took the extraordinary step of affording the heretofore non-active participants in this docket an opportunity to file, no later than April 17, 2000, written comments concerning the proposed settlement.

By letter dated April 17, 2000, counsel for DEUG informed me that DEUG had 'elected not to file written comments concerning the proposed settlement.' Also by letter dated April 17, 2000, Enron's counsel contended that the proposed settlement did not address rules governing the use of Delmarva's generating assets by an unregulated affiliate, and argued that a 'Genco' Code of Conduct was necessary.

At the conclusion of the hearing, the evidentiary record consisted of 11 exhibits and a 46-page verbatim transcript of all proceedings thus far. As there were no matters in dispute, briefs were deemed unnecessary. The parties jointly submitted for my consideration proposed findings and recommendations, which I have substantially incorporated herein. I have also considered the entire record of this proceeding. Based thereon, I submit for the Commission's consideration these Findings and Recommendations.

III. *THE ISSUES*

The issues to be decided in this docket relate to the appropriateness of Delmarva's proposed Cost Accounting Manual and Code of Conduct. The proposed settlement of these issues by the actively participating parties to the docket raises the ultimate issue of whether the proposed settlement is in the public interest pursuant to 26 *Del. C.* §512(c).

IV. *SUMMARY OF EVIDENCE AND DISCUSSION*

Introduction

The purpose of codes of conduct and cost accounting manuals is to assure that the unregulated affiliate does not gain an undue, unique advantage in the competitive marketplace by virtue of its affiliation with a regulated utility in the same marketplace. Examples of such advantages include: the provision of utility customer information to an affiliate when that information is not available to other competitors; cross-subsidization caused by shifting costs from the competitive enterprise to customers of the regulated utility; preferences in the application of utility rules; and tying between utility services and services of an affiliate. (*See* Ex. 2 (Wathen) at 4-5; Ex. 9 (Crane) at 18.)

The Commission first approved a Code of Conduct and Cost Accounting Manual for Delmarva in PSC Docket No. 97-65. More recently, by Order No. 5218 in Docket No. 98-424, the Commission directed the Company to file a new proposed CAM and Code to govern activities and interactions between regulated and unregulated divisions, affiliates, subsidiaries, and the parent of Delmarva. The Commission's Order directed that:

In drafting these new proposed Cost Accounting Manual and Code of Conduct, the Company should consider: (a) the determinations made by the Commission in PSC Findings, Opinion, and Order No. 4706; (b) the requirements imposed by the 'Electric Restructuring Act of 1999' (72 Del. Laws c. 10); (c) the positions of the parties in PSC Docket No. 99-163; and (d) the audit reports to be filed under PSC Orders No. 4706 and 4768.
(Order No. 5218 at ¶ 7.)

Cost Accounting Manual

Even before the parties reached the proposed settlement, the Settling Parties agreed that the Company's proposed CAM contains the necessary information, stated with sufficient clarity, to separate regulated and unregulated costs. (Ex. 5 (Lavin) at 3; Ex. 9 (Crane) at 7-8; Ex. 11 (Stright) at 3-4, 7-8.) Mr. Lavin noted that audits by Deloitte & Touche ('D&T'), attached as exhibits to his pre-filed testimony, 'affirm that Conectiv and [Delmarva] have maintained effective internal controls over the assignment of costs based on the policies and procedures contained within its CAM... .' (Ex. 5 (Lavin) at 11.) Dr. Barua noted that Staff has not received any complaints about Delmarva's operation under the CAM. (Ex. 10 (Barua) at 6.)

Mr. Stright recommended modifications in audit and reporting procedures. At the hearing he testified that his recommendations have been addressed by the proposed settlement. (Tr. at 42-43.)

Code of Conduct

Mr. Wathen described and supported the Company's proposed revised Code. His testimony included an account of the history of the Code and the Company's experience while operating under the CAM and Code that were approved in Docket No. 97-65. He testified that the Company established an extensive training process to implement the Code; specific training materials are attached as Exhibit JMW-2 to Mr. Wathen's pre-filed direct testimony. (Ex. 2)

Mr. Wathen further testified that D&T had conducted an audit of the implementation of the Code, which was submitted to the Commission on July 9, 1999. (*Id.* at 4.) The report noted that the training provided by Delmarva was consistent with that required by the Code. The D&T audit reports are attached to Mr. Lavin's testimony as Schedules JPL-3 through JPL-5. According to the D&T report, there have been no abuses of the Code by Delmarva or its affiliates, nor has there been inappropriate steering. Mr. Wathen testified that there have been no complaints about abuses of the Code by the Company. (Ex. 2 (Wathen) at 4.)

In conclusion, Mr. Wathen testified that the evidence shows that the Code has been operating efficiently since January 1998, as designed, and that the existing Code adequately prevents undue advantage from accruing to a competitive affiliate of the regulated utility. (*Id.*) He, therefore, proposed a slightly modified Code of Conduct, which he attached as Exhibit JMW-1 to his testimony. (*Id.*)

Dr. Kahn testified that principles of efficient competition should inform the Commission's formulation of codes of conduct. On the one hand, he suggested that the Commission should protect against tying and cross-subsidization; but on the other hand, he urged that the Commission not deny the Company and its customers legitimate benefits of integration. Dr. Kahn testified that he believed that the existing Code was sufficient to protect ratepayers and that, indeed, it may restrict more activity than necessary to achieve that end. (Exhibits 7 and 8.)

Dr. Barua testified that Staff has received no complaints about Delmarva's operation under the existing Code. (Ex. 10 (Barua) at 3, 6.) Furthermore, he stated, Staff finds the Company's proposed Code acceptable. (*Id.* at 4.) Dr. Barua also noted that he saw no need at present for a generation company ('Genco') Code of Conduct. (*Id.* at 5.) He also recommended that competitive businesses be transferred out of the legal entity Delmarva Power & Light Company by August 2000. (*Id.*)

Ms. Crane disagreed with Mr. Wathen and Dr. Kahn on a number of points. Her recommendations included the following (Ex. 9 at 3-4):

• Services provided by the shared services company, Conectiv Resource Partners, Inc., should be limited to common support services. Conectiv Resource Partners should not provide customer service or marketing services, nor should it provide services that only benefit either regulated or non-regulated entities.

• Delmarva should not share directors or officers with non-regulated subsidiaries.

• The Commission should adopt asymmetrical pricing for services between regulated and non-regulated entities, as well as for asset transfers. Common services provided by Conectiv Resource Partners should be priced at fully distributed cost.

• Delmarva's proposed Code of Conduct should be modified to:

a. Prohibit the release of any customer information without the written consent of the customer.

b. Prohibit sales leads.

c. Incorporate the Codes of Conduct adopted by other states with jurisdiction over Delmarva.

• Delmarva's proposed Code of Conduct should be expanded to:

a. Prohibit joint sales calls, joint promotions, and joint advertising.

b. Require physical separation of regulated and non-regulated operations.

c. Require similar treatment of competitors and affiliates with regard to fee waivers and rebates.

d. Limit Delmarva's ability to use regulated utility revenues and assets to finance competitive activities.

• The Commission should adopt the Code of Conduct recommended by the DPA and provided in Appendix C to Ms. Crane's testimony.
(Ex. 9 (Crane) at 3-4.)

The Proposed Settlement

Provisions Relating To The Cost

Accounting Manual

Cost Accounting Manual. The settlement provides that the Cost Accounting Manual filed by the Company on November 15, 1999, and modified as discussed herein, should be approved to govern the allocation of the charges of cost between the Company and Conectiv's unregulated products and services. (Ex. 4 at ¶ II.A.1.) The modifications include moving certain provisions from exhibits into the body of the Cost Accounting Manual and adding a specific description of employee time record keeping applicable to Conectiv employees.

Audits. The settlement provides for an audit to be conducted once every three years. (*Id.* at ¶ II.A.2.) The first audit will be performed in 2002 and will cover the year 2001. However, if another state commission having jurisdiction over the Company requires audits on a different schedule, the Company has the option to coordinate the timing of the audits, with appropriate notice to Staff and the DPA. These audits will be similar in nature and scope to the 1997 and 1998 Schedule of Non-regulated Expenses and Affiliate Transactions of Delmarva required in Docket No. 97-65. The Staff and the Public Advocate will have an advisory role in selecting the external auditor to be used in those audits, but Delmarva will make the final selection of the external auditor.

Asymmetrical Pricing. The settlement also provides for asymmetrical pricing for transfers of services between the Company and competitive activities. (*Id.* at 4.) Transfers from the Company to an affiliate will be at the higher of fully allocated cost or market, while transfers from competitive affiliates to the Company will be at the lower of fully allocated cost or market. If market value is not reasonably ascertainable, fully allocated cost will be used. Asymmetrical pricing will not apply to transfers between the Company and the shared service company, Conectiv Resource Partners.

Finally, Delmarva will submit a revised CAM, consistent with the foregoing changes, within 60 days of a Commission Order adopting the recommendations set forth herein. (*Id.* at ¶ II.A.4.)

Provisions Relating To The Code Of Conduct

Joint Promotions. The Company will not engage in any joint advertising, or joint promotions involving Regulated Utility Activities and Affiliated Supplier Services. (*Id.* at ¶ II.B.2.) Regulated Utility Activities Personnel are prohibited from participating with Affiliated Suppliers in sales calls or other meetings with regulated utility customers unless they also participate in such meetings with Third-Party Suppliers on the same terms and conditions on a non-discriminatory basis. (*Id.* at ¶ II.B.3.) The settlement requires that the Company maintain records of such meetings for three years from the date of the settlement and make those records available for inspection upon request. (*Id.*)

Discounts — Equal Availability. The Company must also offer similarly situated third parties the same discounts, rebates, fee waivers or penalty waivers with respect to Regulated Utility Services that are or might be provided to an affiliate. (*Id.* at ¶ II.B.4.)

Sales Leads. Under the terms of the settlement and the Code, Regulated Utility Activities Personnel will not be permitted to provide Supply Sales Leads to any Competitive Activities. (*Id.* at ¶ II.B.5)

Separate Operational Personnel. The settlement provides that operational personnel up to and including vice presidents directly responsible for regulated operations will be different individuals from the operational personnel for Affiliated Supplier Services. (*Id.* at ¶ II.B.6.) This provision does not apply to officers at the Senior Vice President level and above or to members of the Board of Directors.

Shared Facilities. The settlement allows for the common use of facilities, equipment, and computer systems; but only with appropriate safeguards and security measures to prevent the access by competitive ventures of information or data of the regulated utility in violation of the Code. (*Id.* at ¶ II.B.7.)

Customer Care and Marketing. The settlement allows for customer care and marketing functions to remain in the shared services company, but requires that the Affiliated Supplier Services have separate marketing managers and organizations within that function. (*Id.* at ¶ II.B.8.) There is a similar requirement for separate customer care managers and organizations. (*Id.*)

Customer Information. Consistent with the Code that was previously approved by the Commission in Docket No. 97-65, all utility Customer Information will be considered as being confidential. (*Id.* at ¶ II.B.9.) Customer Information will be released only with the explicit written approval of the customer and only to the party or parties that are approved and for the purposes approved by the customer.

Field Contact Compliance Check. The Company will continue to make follow-up compliance phone calls for any Field Contacts with Regulated Utility Activities Personnel during which the customer requested a list of Third-Party Suppliers for any competitive service. (*Id.* at ¶ II.B.10.) This is to assure that the Company's employees are complying with the Code. This follow-up will be done on a quarterly basis with a sampling of approximately 10 percent of the Field Contact customers that requested the supplier list.

Use of Delmarva Power Name. The settlement prohibits the use of the name Delmarva Power or Delmarva Power & Light and any logo using those names to be used as a trade name for any Competitive Activities for a period of two years. In the case of an Affiliated Supplier, the prohibition extends for a 10-year period. (*Id.* at ¶ II.B.11.)

Removal of Competitive Activities From Delmarva Power & Light Company. The Company has also agreed in settlement to use its best efforts to remove all Competitive Activities from the legal entity Delmarva Power & Light Company and to put them in separate affiliated entities by August 31, 2000. (*Id.* at ¶ II.C.1.)

Semi-Annual Employee Transfer Reports. The settlement also requires the Company, for a period of two years, to file semi-annual reports showing transfers of employees between Competitive Activities and both the Company and Conectiv Resource Partners, Inc., the shared service company. (*Id.* at ¶ II.C.2.)

PUHCA. Lastly, the parties agree that the Public Utility Holding Company Act ('PUHCA') presently provides adequate protection against the abuse of the use of utility assets for the benefit of competitive affiliates. In the event that PUHCA is repealed, however, the proposed settlement provides that the parties will negotiate in good faith to determine whether similar provisions to those provided by the Act should be adopted by the Commission to provide the same type of protections. (*Id.* at ¶ II.C.3.)

Discussion

The Delaware General Assembly has mandated that the Commission should encourage the resolution of matters before it by settlement and that the Commission may approve such settlements, whether or not all parties agree to them. 26 *Del. C.* §512.

The witnesses who testified at the hearing agreed that the proposed settlement is in the public interest. Mr. Wathen testified that the settlement 'accomplishes the objective of what the Commission had asked for, which was to look at and consider the Code of Conduct and Cost Accounting Manual in light of energy competition, both gas and electricity, in Delaware.' (Tr. at 22-23.)

Ms. Crane testified that the settlement is in the public interest and, specifically, that it provides suitable protection to ratepayers on the issues of: shared employees and facilities; asymmetrical pricing; confidentiality of customer information; provision of vendor lists to customers; sales leads; equal treatment for third parties and competitive affiliates on fee waivers; and use of the name Delmarva Power & Light Company. (*Id.* at 30-36.)

Dr. Barua testified that he participated in the negotiation of the proposed settlement; that it adequately addresses the issues raised by Staff in connection with the Code of Conduct; and that the settlement should be approved as in the public interest. (*Id.* at 38-39.)

Mr. Stright testified that the proposed settlement addresses all three areas that he raised on behalf of Staff with respect to the Cost Accounting Manual (auditing, reporting requirements, and structure and content of the CAM) and that the proposed settlement is in the public interest. (*Id.* at 42-43.)

1. As noted above, the other parties to the case declined to file testimony in this case or to appear at the hearing to cross-examine the witnesses of the Settling Parties. All parties were afforded an opportunity to review and comment on the proposed settlement before and after the settlement. On April 17, 2000, Enron filed comments on the proposed settlement. Enron asserted that '[a] 'Genco' Code of Conduct is necessary to provide minimal protections against the anti-competitive use of Delmarva's generation assets' and that 'such a Genco Code should include the following:'

- A requirement that the Genco not discriminate in the terms and conditions of any transactions with affiliates, *i.e.*, that such conditions be available on identical terms to non-affiliates.

- A requirement that the Genco functionally separate its operations and personnel to assure no cross-subsidy and no exchange of data and/or information with the Genco.

- A requirement that Genco operate in the wholesale market, rather than making sales directly to retail customers.

Enron's comments note that such provisions were agreed to by certain utilities in other states, but the comments do not cite any evidence in this record or Delaware law indicating that such provisions are necessary or appropriate in this State.

Moreover, pursuant to the Act, '[e]3xcept as otherwise expressly provided for in this chapter, on and after October 1, 1999 for DP&L ... the generation, supply and sale of electricity, including all related facilities and assets, shall no longer be regulated by the commission as a public utility service or function.' 26 *Del. C.* § 1003(a). This provision converts a Genco from a regulated utility activity into a competitive activity. On this basis, Delmarva argues, promulgating a Genco Code purporting to govern the relationship between the deregulated Genco and the other competitive activities would be outside the Commission's jurisdiction. (Ex. 7 (Kahn) at 35.)

Dr. Kahn further testified that there is no reason for Commission concern about cross-subsidization of one unregulated venture by another and that it would be anti-competitive to prohibit the Company's generation affiliate from operating in the state. (*Id.* at 36-37.)

I reach no conclusions with respect to these legal and policy issues because there is no evidence in this record to support adoption of a special code for generation assets. As both Dr. Kahn and Dr. Barua point out, the general Code of Conduct is broad enough to cover the Company's relationship with its generation affiliate, as with its other unregulated affiliates. (Ex. 7 (Kahn) at 35; Ex. 10 (Barua) at 5.) As Dr. Barua further testified, 'Staff is not aware at this time of any questionable activities by utilities that do not have GENCO codes.' (Ex. 10 (Barua) at 5.) PJM market rules also will provide discipline to the market. (*Id.*)

I also find it unnecessary to undertake to draft a 'Genco' code because there is no evidence in this record that one is warranted.

Based upon the entire record and upon the terms of the proposed settlement itself, I find that the settlement is in the public interest. Among the considerations supporting this conclusion are the following:

a. The parties agree that it is appropriate for the relationship between Conectiv's regulated utility activities and competitive activities to be governed by a CAM and Code;

b. The parties agree and the undisputed evidence establishes that the existing CAM, as modified by the settlement, is adequate for the task of allocating costs between regulated and unregulated activities;

c. Independent audits indicate that the Company has complied with the existing Code and CAM;

d. Staff has received no complaints to the contrary, and there is no evidence to the contrary in the record;

e. The proposed settlement has been negotiated and agreed to by the three actively involved parties to the litigation;

f. The witnesses at the hearing agreed that the resolution of issues in the proposed settlement is in the public interest;

g. The proposed settlement constitutes a reasonable negotiated settlement of disputed policy issues that will reduce the expense of fully litigating the issues; and

h. The proposed settlement considers the determinations made by the Commission in: (i) Findings, Opinion, and Order No. 4706; (ii) the requirements of the 'Electric Restructuring Act of 1999;' (iii) the positions of the parties in Docket No. 99-163; and (iv) the audit reports filed pursuant to Commission Orders No. 4706 and 4768.

V. *RECOMMENDATIONS*

In summary, and for the reasons discussed above, I propose and recommend to the Commission the following:

A. That the Commission find that the proposed settlement is in the public interest and, accordingly, approve it;

B. That the Commission approve the proposed Code of Conduct attached to the settlement;

C. That the Commission not adopt a Genco Code of Conduct;

D. That the Commission approve the proposed Cost Accounting Manual as modified pursuant to the settlement; and

E. That, within 60 days of a Commission Order approving the recommendations made herein, the Company serve and file a revised Cost Accounting Manual reflecting the changes agreed to in the settlement.

ATTACHMENT 'A'

PROPOSED SETTLEMENT

On this day, April 5, 2000, Delmarva Power & Light Company, d/b/a Conectiv Power Delivery (the 'Company' or 'CPD'), and the other undersigned parties (all of whom together are the 'Settling Parties') hereby propose a settlement that, in the Settling Parties' view, appropriately resolves all issues raised in this proceeding.

I. *INTRODUCTION*

1. In Docket No. 98-424, Order No. 5218, the Commission directed the Company to file, by November 15, 1999, a new proposed Cost Accounting Manual (the 'CAM ') and proposed Code of Conduct (the 'Code') to govern: (a) the allocation of costs between Conectiv Power Delivery's regulated utility services and Conectiv's unregulated products; and (b) the course of conduct between Conectiv Power Delivery's regulated divisions and Conectiv's competitive divisions, subsidiaries and affiliates.

2. On November 15, 1999, CPD made such filing, which included the testimony of (a) J. Mack Wathen, Director of Finance and Regulatory Affairs for Conectiv, and his exhibits, which included the Company's new proposed Code of Conduct; (b) James P. Lavin, Controller for Conectiv, and his exhibits, including CPD's new proposed Cost Accounting Manual; and (c) Dr. Alfred E. Kahn, the Robert Julius Thorne Professor of Political Economy, Emeritus, Cornell University and Special Consultant with National Economic Research Associates, Inc., which was for the purpose of responding to the positions of parties in PSC Docket No. 99-163 and evaluating the effectiveness of the current Code of Conduct adopted by the Commission in PSC Docket No. 97-65.

3. As directed by the Commission in Order No. 5218, copies of the filing were provided to all individuals on the service list, which included the Division of the Public Advocate, each entity or person appearing on the Service List in PSC Docket No. 97-65 and those appearing on the Service List in PSC Docket No. 99-163.

4. On December 1, 1999, in Order No. 5293, the Commission opened this docket and assigned the matter to Hearing Examiner G. Arthur Padmore for further proceedings, and directed that notice be given.

5. Pursuant to such Order, notice, including information on how to intervene in the proceeding, was published on December 8 and 9, 1999, in both The News Journal and the Delaware State News. A number of parties intervened: in addition to the Company, Commission Staff and the Division of the Public Advocate ('DPA'), the parties in this docket are: the Delaware Energy Users Group; Cable Telecommunications Association of Maryland, Delaware & DC; the Mid-Atlantic Power Supply Association; Shell Energy Services Company, LLC; and Enron Capital and Trade Resources, Inc.

6. On March 6, 2000, Staff filed the direct testimony of witnesses Robert L. Stright of Liberty Consulting and Rajnish Barua, the Commission's Regulatory Policy Administrator. On the same date, the DPA filed the direct testimony of witness Andrea C. Crane of The Columbia Group, Inc. On March 29, 2000, the Company filed the rebuttal testimony of Messrs. Wathen and Lavin, and Dr. Kahn. None of the other parties to this proceeding filed testimony.

7. Capitalized terms used in this Proposed Settlement without definition shall have the meanings ascribed to them in the Code attached as Exhibit A hereto (the 'Recommended Code').

II. *SETTLEMENT PROVISIONS*

A. *COST ACCOUNTING MANUAL PROVISIONS*

1. The Settling Parties agree that the CAM filed on November 15, 1999, as Schedule JPL-6 to the direct testimony of James P. Lavin, should be approved by the Commission to govern the allocation of costs between Conectiv Power Delivery's regulated utility products and services and Conectiv's unregulated products and services, with only the modifications specifically addressed herein.

2. The Settling Parties agree that audits shall be conducted every third year with the next audit occurring in 2002, covering the year 2001; provided, however, that if another state commission having jurisdiction over the Company requires audits on a different schedule, the Company shall have the option to coordinate the Delaware audits required by this Settlement with the timing of audits required by such other states, with appropriate notice to Staff and DPA. Further, these audits shall be similar in nature and scope to the 1997 and 1998 Schedule of Nonregulated Expenses and Affiliate Transactions of Delmarva required under Docket No. 97-65. The Settling Parties also agree that Staff and DPA shall have an advisory role in the selection of the independent auditor, but ultimately the selection of the independent auditor shall be in the discretion of the Company.

3. The Company agrees that it will specifically describe the employee time-recordkeeping applicable to Conectiv employees in the CAM. CPD further agrees that it will make the following cosmetic changes to the CAM recommended by Staff: the Company will move the 'guiding principles,' currently contained in Exhibit 10 to the CAM, to an introductory section of the CAM; and the Company will clearly set forth the pricing rules for asset transfers, which are currently contained in Exhibit 4 to the CAM, in the text of the CAM.

4. The Settling Parties agree that, for transfers of services between Conectiv Power Delivery and Competitive Activities, asymmetrical pricing principles (*i.e.*, for transfers from Conectiv Power Delivery to a Competitive Activity, the higher of fully allocated cost or market price; for transfers from a Competitive Activity to Conectiv Power Delivery, the lower of fully allocated cost or market price) shall apply; provided, however, that such asymmetrical pricing principles shall not apply to transfers of services between Conectiv Resource Partners, Inc. and Conectiv Power Delivery; and provided, further, that if the market price of such services is not reasonably ascertainable, fully allocated cost will be used. A revised CAM reflecting these changes will be filed within 60 days after the date of issuance by the Commission of a final order approving this Proposed Settlement.

B. *CODE OF CONDUCT PROVISIONS*

1. The Settling Parties agree that the attached Recommended Code should be approved by the Commission to govern the course of conduct between Conectiv Power Delivery's regulated divisions and Conectiv's competitive divisions, subsidiaries and affiliates. This Settlement Proposal addresses, and the Recommended Code reflects, modifications made, as part of this Settlement, to the Code filed on November 15, 1999, as Exhibit JMW-1 to the direct testimony of J. Mack Wathen.

2. The Settling Parties agree that Conectiv Power Delivery shall not engage in any joint advertising or joint promotions involving both Regulated Utility Activities and Affiliated Supplier Services; provided, however, that this prohibition shall not be construed to prohibit the use of similar names and logos (subject to the prohibition on the use of the name 'Delmarva Power' or 'Delmarva Power & Light Company' for Competitive Activities discussed below), nor shall it be construed to prohibit brand and image advertising.

3. The Settling Parties agree that Regulated Utility Activities Personnel shall not participate with Affiliated Suppliers in sales calls or other meetings with customers of Regulated Utility Activities, unless Regulated Utility Activities Personnel

also participate with Third-Party Suppliers, on a non-discriminatory basis and on the same terms and conditions, in such sales calls or other meetings with customers of Regulated Utility Activities. Moreover, for a period of three years from the time this Proposed Settlement is approved by the Commission, Conectiv Power Delivery shall keep records showing each sales call or other meeting with a customer of Regulated Utility Activities in which a Regulated Utility Personnel representative participated along with either an Affiliated Supplier or a Third-Party Supplier. Such reports shall detail the date of the sales call or other meeting, the name and address of the customer, the identity of the Regulated Utility Activities Personnel representative attending such sales call or other meeting, and the identity of the Affiliated Supplier or Third-Party Supplier attending such sales call or other meeting. This reporting obligation shall cease at the end of the three-year period, unless the Commission Staff, the Department of the Public Advocate and the Company agree on the need to continue this reporting requirement beyond such period.

4. The Settling Parties agree that Conectiv Power Delivery shall offer to all similarly situated Third Parties or customers of Third Parties the same discounts, rebates, fee waivers, or penalty waivers with respect to Regulated Utility Services that it may offer to a Competitive Activity or customers of a Competitive Activity.

5. The Settling Parties agree that Regulated Utilities Activities Personnel shall not provide Supply Sales Leads to any Competitive Activity.

6. The Settling Parties agree that operational personnel for Regulated Utility Activities, up to and including the Vice President(s) directly responsible for Regulated Utility Activity operations, shall be different individuals from the operational personnel for Affiliated Supplier Services, up to and including the Vice President(s) directly responsible for Affiliated Supplier Services operations, and that such individuals shall not be shared among Regulated Utility Activities and activities for Affiliated Supplier Services. This sharing prohibition shall not apply to officers at the Senior Vice President level and above, or to members of Boards of Directors.

7. The Settling Parties agree that Regulated Utility Activities and Competitive Activities shall be allowed to share office space, office equipment, services and systems, and that each can access the computer or information systems of the other, so long as adequate security and system protections are in place to prevent the accessing of information or data of Regulated Utility Activities by Competitive Activities that would be in violation of other provisions of the Recommended Code. The Company agrees to allow each of the Commission Staff and the Department of the Public Advocate the opportunity to review such security and system protections periodically upon its request, at times to be mutually agreed upon by such requesting party and the Company.

8. The Settling Parties agree that customer care and marketing functions may remain in the shared service company, but that Conectiv Power Delivery shall have a manager (below the Vice President level) for the marketing functions for Regulated Utility Activities, who is a different individual from the manager (below the Vice President level) for marketing functions for Affiliated Supplier Services. Moreover, Conectiv Power Delivery shall have a manager (below the Vice President level) for customer care functions for Regulated Utility Activities, who is a different individual from the manager (below the Vice President level) for customer care functions for Affiliated Supplier Services.

9. The Settling Parties agree that the Recommended Code shall have the same provisions regarding the confidentiality of utility customer information as were contained in the Code of Conduct approved by the Commission in Docket No. 97-65.

10. The Settling Parties agree that Conectiv Power Delivery shall, on a quarterly basis, place a follow-up telephone call to a random sample of approximately 10% of the customers who requested a list of Third Parties during a Field Contact during the previous quarter, for the purpose of ascertaining whether the employee complied with Section B.10(a), (b) and (c) of the Code during the Field Contact. Records of these telephone calls shall be retained for a period of two years, and records of such telephone calls shall be produced for inspection upon Commission request.

11. The Settling Parties agree that the name 'Delmarva Power' or 'Delmarva Power & Light Company' and any logo using those names, shall not be used as the legal name or the trade name for any Competitive Activity for a period of two years from the time this Proposed Settlement is approved by the Commission; provided, however, that the name 'Delmarva Power' or 'Delmarva Power & Light Company' and any logo using those names, shall not be used as the legal name or the trade name for any Affiliated Supplier Services for a period of ten years from the time this Proposed Settlement is approved by the Commission.

C. *MISCELLANEOUS PROVISIONS*

1. The Company agrees to use its best efforts to remove all competitive services from the legal entity of Delmarva Power & Light Company and transfer them to separate affiliated entities by August 31, 2000; provided that (a) nothing herein will affect the planned sale of generation facilities, including the planned sale in September or thereafter of fossil units to NRG Energy, Inc.; (b) subject to Sections 14 and 15 of the Recommended Code, Delmarva Power employees shall continue to be allowed to perform work for Competitive Activities, so long as such employees comply with the Code provisions and their time is properly charged; and (c) certain short-term wholesale power sales and wholesale power purchase master agreements and transactions that will expire, by their terms, on September 1, 2000, shall not be so transferred, but shall be allowed to expire.

2. The Settling Parties agree that, for a period of two years from the time this Proposed Settlement is approved by the Commission, Conectiv Power Delivery shall file semi-annual reports showing transfers of employees made: (a) from Conectiv Power Delivery to Competitive Activities; (b) from Competitive Activities to Conectiv Power Delivery; (c) from Conectiv Resource Partners, Inc. to Competitive Activities; and (d) from Competitive Activities to Conectiv Resource Partners, Inc. These reporting obligations shall cease at the end of the two-year period, unless the Commission Staff, the Department of the Public Advocate and the Company agree on the need to continue this reporting requirement beyond such period; provided that, if the parties cannot agree and any of such parties believes the reporting obligations should continue, such party may submit the issue to the Commission for resolution.

3. The Settling Parties agree that the Public Utility Holding Company Act of 1935 ('PUHCA') provides adequate protections against the abuse of utility assets for the benefit of non-utility activities. If PUHCA is repealed in the future, the Settling Parties agree that they will negotiate in good faith to determine whether similar provisions should be adopted by the Commission to provide similar protections.

D. *Standard Provisions and Reservations*

1. The provisions of this Proposed Settlement are not severable.

2. This Proposed Settlement represents a compromise for the purposes of settlement and shall not be regarded as a precedent with respect to any ratemaking or any other principle in any future case or in any existing proceeding, except that, consistent with and subject to the provisos of sub-paragraph II.D.8 below, this Proposed Settlement shall preclude any Settling Party from taking a contrary position with respect to the issues specifically addressed and resolved herein and in the Recommended Code, in proceedings involving the review of this Proposed Settlement and any appeals related to this Proposed Settlement. No Party to this Proposed Settlement necessarily agrees or disagrees with the treatment of any particular item, any procedure followed, or the resolution of any particular issue in joining in this Proposed Settlement other than as specified herein, except that each Settling Party agrees that the Proposed Settlement may be submitted to the Commission for a determination that it is in the public interest and that no Settling Party will oppose such a determination. Except as set forth in sub-paragraph II.D.8. below, none of the Settling Parties waives any rights

that it may have to take any position in future proceedings regarding the issues in this proceeding, including positions contrary to positions taken herein or previously taken.

3. In the event that this Proposed Settlement does not become final either because it is not approved by the Commission, or because it is the subject of a successful appeal and remand, each of the Settling Parties reserves its rights to submit additional testimony, file briefs, or otherwise take positions as it deems appropriate in its sole discretion to litigate the issues in this proceeding.

4. The Proposed Settlement will become effective upon the Commission's issuance of a final order approving this Proposed Settlement and all the settlement terms and conditions without modification. After the issuance of such final order, the terms of this Proposed Settlement shall be implemented and enforceable notwithstanding the pendency of a legal challenge to the Commission's approval of this Proposed Settlement or to actions taken by another regulatory agency or Court, unless such implementation and enforcement is stayed or enjoined by the Commission, another regulatory agency, or a Court having jurisdiction over the matter.

5. The obligations under this Proposed Settlement that apply for a specific term set forth herein shall expire automatically in accordance with the term specified, and shall require no further action for their expiration.

6. The Settling Parties may enforce this Proposed Settlement through any appropriate action before the Commission or through any other available remedy. The Settling Parties shall consider any final Commission order related to the enforcement or interpretation of this Proposed Settlement as an appealable order to the Superior Court of the State of Delaware. This shall be in addition to any other available remedy at law or in equity.

7. If a Court grants a legal challenge to the Commission's approval of this Proposed Settlement and issues a final non-appealable order which prevents or precludes implementation of any material term of this Proposed Settlement, or if some other legal bar has the same effect, then this Proposed Settlement is voidable upon written notice by any of the Settling Parties.

8. This Proposed Settlement resolves, with prejudice, all of the issues specifically addressed herein and in the Recommended Code, and precludes the Settling Parties from asserting contrary positions during subsequent litigation in this proceeding or related appeals; provided, however, that this Proposed Settlement is made without admission against or prejudice to any factual or legal positions which any of the Settling Parties may assert (a) in the event that the Commission does not issue a final, non-appealable order approving this Proposed Settlement without modification; or (b) in other proceedings before the Commission or other governmental body so long as such positions do not attempt to abrogate this Proposed Settlement. The Settling Parties agree that this Proposed Settlement shall not constitute or be cited as controlling precedent in any other proceedings, including other proceedings before the Commission or before any other governmental body in the State of Delaware or elsewhere. This Proposed Settlement is determinative and conclusive of all of the issues addressed herein and, upon approval by the Commission, shall constitute a final adjudication as to the Settling Parties of all of the issues in this proceeding.

9. This Proposed Settlement is expressly conditioned upon the Commission's approval of all of the specific terms and conditions contained herein without modification. If the Commission should fail to grant such approval, or should modify any of the terms and conditions herein, this Proposed Settlement will terminate and be of no force an effect, unless the Settling Parties agree to waive the application of this provision. The Settling Parties will make their best efforts to support this Proposed Settlement and to secure its approval by the Commission.

10. It is expressly understood and agreed that this Proposed Settlement constitutes a negotiated resolution of the issues in this proceeding and any related court appeals.

III. *CONCLUSION*

IN WITNESS WHEREOF, intending to bind themselves and their successors and assigns, the undersigned parties have caused this Proposed Settlement to be signed by their duly-authorized representatives.

PROPOSED NEW CODE OF CONDUCT

GOVERNING REGULATED UTILITY

ACTIVITIES AND COMPETITIVE

ACTIVITIES

A. *Definitions*

Capitalized terms in the Code of Conduct shall have the following meanings:

1. 'Affiliated Suppliers' shall mean a Competitive Activity which is also duly licensed by the Commission to provide electricity or natural gas supply services to retail customers within Conectiv Power Delivery's regulated service territory in Delaware.

2. 'Affiliated Supplier Services' shall mean electricity or natural gas supply services offered to retail customers by an Affiliated Supplier within Conectiv Power Delivery's regulated service territory in Delaware.

3. 'Bill' shall mean the billing invoice for Regulated Utility Services.

4. 'Competitive Activities' shall mean any business activities of Delmarva or its affiliates that are not Regulated Utility Activities.

5. 'Conectiv Power Delivery' shall mean any operations within Delaware of Delmarva Power & Light Company doing business under the trade name Conectiv Power Delivery (or any successor trade name for such operations), specifically, the Regulated Utility Activities of Delmarva Power & Light Company.

6. 'Customer Information' shall mean any customer-specific information obtained as a direct result of Conectiv Power Delivery's providing Regulated Utility Services.

7. 'Delmarva' shall mean any operations of Delmarva Power & Light Company, or any successor, that are not Regulated Utility Activities.

8. 'Extraordinary Circumstance' shall mean any of the following, or similar, situations which require any action contrary to this Code of Conduct: (a) an abnormal system condition requiring manual or automatic action to maintain system frequency, or to prevent loss of firm load, equipment damage, disconnection of system elements that could adversely affect the reliability of Conectiv Power Delivery's electric system or natural gas system or the safety of persons or property; or (b) a fuel shortage requiring departure from normal operating procedures in order to minimize the use of a particular fuel; (c) a condition that requires implementation of emergency procedures as defined in the Pennsylvania-New Jersey-Maryland Interconnection Association Manual; (d) a condition described in Conectiv Power Delivery's Gas Tariff to which the emergency or curtailment procedures set forth in the Gas Tariff apply; or (e) an applicable law or regulation, or an order or directive by a court or regulatory agency having jurisdiction over Delmarva or Conectiv Power Delivery or an affiliate.

9. 'Field Contact' shall mean any face-to-face meeting between any Regulated Utility Activities Personnel and a customer at a location outside of an office facility used for Regulated Utility Activities (including at the customer's home or business, or at a location where Regulated Utility Activities Personnel are reading meters related to Regulated Utility Activities, making installations for Regulated Utility Services, or maintaining outside Regulated Utility Activities plant or equipment).

10. 'Regulated Utility Activities' shall mean, at any given time, any of Conectiv Power Delivery's operations subject by law to regulation by, and the ratemaking authority of, any state utility commission or the Federal Energy Regulatory Commission ('FERC').

11. 'Regulated Utility Activities Personnel' shall mean any Conectiv Power Delivery personnel who are, at the time in question, performing work as part of providing Regulated Utility Services.

12. 'Regulated Utility Services' shall mean any services offered to customers by Conectiv Power Delivery as part of its Regulated Utility Activities and for which any state utility commission or the FERC sets or approves the rates that may be charged by Conectiv Power Delivery to its customers.

13. 'Sales Lead' shall mean any information obtained by Regulated Utility Activities Personnel from a customer of Regulated Utility Services regarding a potential sale to the customer of a Competitive Activities product or service.

14. 'Same Terms' with respect to the provision of any Regulated Utility Activities-related product or service, shall mean on the same terms and conditions as the provision thereof is made to Competitive Activities (and without the incurrence of any additional cost by Regulated Utility Activities than would have been incurred in the provision of such product or service to Competitive Activities — any such additional costs to be borne by any Third Party requesting the provision of such product or service).

15. 'Supply Sales Lead' shall mean any information obtained by any Regulated Utility Activities Personnel from a customer of Regulated Utility Services regarding a potential sale to the customer of an Affiliated Supplier Service.

16. 'Third Party,' individually, and 'Third Parties,' collectively, shall mean any business enterprise that does not fall within the definition of Regulated Utility Activities or Competitive Activities.

17. 'Third-Party Supplier,' individually, and 'Third-Party Suppliers,' collectively, shall mean any business that does not fall within the definition of Regulated Utility Activities or Competitive Activities, which is also duly licensed by the Commission to provide electricity or natural gas supply services to retail customers within Conectiv Power Delivery's regulated service territory in Delaware.

B. *Code of Conduct*

The following rules shall apply to transactions between Regulated Utility Activities and Competitive Activities, except in any circumstances where an Extraordinary Circumstance requires a deviation from any such provision, as determined by Conectiv Power Delivery in the exercise of its reasonable judgment:

Treatment of Similarly-Situated Persons

1. Conectiv Power Delivery shall apply each tariff provision in the same manner to the same or similarly situated persons, exercising any discretion with due regard for the particular facts and circumstances to which the tariff provision is applied.

2. Conectiv Power Delivery shall process all similar requests for Regulated Utility Services in the same manner and within the same period of time, whether requested on behalf of Competitive Activities or by a Third Party; provided that this provision shall not in any manner be construed to limit Conectiv Power Delivery's ability to carry out its public service obligation as it deems necessary.

3. Conectiv Power Delivery shall offer the same discounts, rebates, fee waivers, or penalty waivers with respect to Regulated Utility Services that it may offer to a Competitive Activity or customers of a Competitive Activity, to all similarly situated Third Parties or customers of Third Parties.

Use of Information

4. Customer Information shall not be provided by Conectiv Power Delivery to Competitive Activities or Third Parties unless the customer to which the Customer Information relates has given express written authorization to do so, and then such information shall be provided by Conectiv Power Delivery only to the extent authorized and only to the person(s) specifically authorized to receive it by the customer.

Use of the Bill; Promotions Within the Bill Envelope

5. Conectiv Power Delivery shall include amounts due for electricity or natural gas supplied to Conectiv Power Delivery customers by Affiliated Suppliers and Third-Party Suppliers, if requested by such Affiliated Suppliers or Third-Party Suppliers, if so specified in the Tariff, Commission Orders or Third-Party Supplier Agreements, and on the terms specified therein.

6. Conectiv Power Delivery shall publish a public notice, in at least 2 State newspapers of general circulation, to notify Third Parties of its determination to include any amounts due for any Competitive Activities (other than electricity or natural gas) on the Bill, which notice shall be published at least 60 days prior to including such amounts on the Bill, and, after such 60-day period, shall include on the Bill amounts due for the products and services of its Competitive Activities and any Third Party on the Same Terms, upon request; provided that this provision shall not prevent Competitive Activities (or any Third Party) from including amounts due for Regulated Utility Services on a bill for Competitive Activities (or a Third Party's products or services, as applicable), so long as the customer receiving such consolidated bill has authorized Competitive Activities (or a Third Party, as applicable) to act as its agent for such purpose.

7. In the event that Conectiv Power Delivery determines to insert any advertising or promotional materials for Competitive Activities into the envelope for the Bill:

(a) Conectiv Power Delivery shall publish a public notice to notify Third Parties of that determination (as well as the type of advertising or promotional material to be inserted) in at least 2 State newspapers of general circulation at least 60 days prior to making such insertion into the envelope for the Bill; and

(b) After such 60-day period, Conectiv Power Delivery shall permit its Competitive Activities and any Third Party to insert advertising or promotional materials of the same general type (*e.g.*, if Conectiv Power Delivery determines to insert help-wanted ads for its Competitive Activities, Third Parties thereafter also may insert help-wanted ads) into the envelope for the Bill upon request, (i) on the Same Terms and (ii) on a fair and non-discriminatory basis.

Customer Telephone Calls

8. Telephone numbers for Regulated Utility Activities shall be different from telephone numbers for Competitive Activities.

Prohibition on Suggestion of Utility Advantage

9. (a) Conectiv Power Delivery shall not state in any advertising, promotional materials or sales efforts, that consumers who purchase products or services from Competitive Activities will receive preferential treatment in the provision of Regulated Utility Services, or that any other advantage regarding the provision of Regulated Utility Services will accrue to customers or others having dealings with Competitive Activities.

a. Conectiv Power Delivery shall not engage in any joint advertising or joint promotions involving both Regulated Utility Activities and Affiliated Supplier Services; provided, however, that nothing herein prohibits the advertising of any Competitive Activities, and nothing herein prohibits Conectiv and the affiliates of Conectiv from engaging in general branding and image advertising, without reference to Third Parties, nor from including in any such advertising factual statements regarding any affiliation with Conectiv Power Delivery or its Regulated Utility Activities, nor from including in any such advertising promotional statements, discounts or other inducements, that are intended to encourage a consumer to use products or services provided by Competitive Activities; provided that such statements, discounts or other inducements are not related to Regulated Utility Services.

(c) Notwithstanding anything in Section 9(a) or (b) above, the name 'Delmarva Power' or 'Delmarva Power & Light Company' and any logo using those names, shall not be used as the legal name or the trade name for any Competitive Activity for a period of two years from the time this Code of Conduct is first approved by the Commission in Docket No. 99-582; provided, however, that the name 'Delmarva Power' or 'Delmarva Power & Light Company' and any logo using those names, shall not be used as the legal name or the trade name for any Affiliated Supplier Services for a period of ten years from the time this Code of Conduct is first approved by the Commission in Docket No. 99-582.

10. (a) Regulated Utility Activities Personnel shall not specify a preference for any Competitive Activities products or services over those of any Third Party, or for any Third Party's products and services over those of any other Third Party. However, such Regulated Utility Activities Personnel may inform customers who inquire about products or services that are not provided as part of Conectiv Power Delivery's Regulated Utility Services that Conectiv Power Delivery's Competitive Activities are suppliers of such products or services, so long as such Regulated Utility Activities Personnel also make the statements set forth below, which: shall be verbal, if the contact with the customer is on the telephone; and shall be verbal and also confirmed by a written form completed by Regulated Utility Activities Personnel if the contact with the customer is a Field Contact. The required statements are as follows:

(i) Similar products or services are available from Third Parties;

(ii) A Commission-maintained list of Third Parties will be supplied by Conectiv Power Delivery to the customer if the customer so desires; and

(iii) The provision of Regulated Utility Services is not in any way contingent upon or tied to the customer's purchase of any products or services provided by Competitive Activities.

(b) If a customer requests, during a contact with Regulated Utility Activities Personnel, a list of Third-Party businesses that supply similar types of products and services as a Competitive Activities product or service, the customer shall be provided the list of Third Parties referred to in paragraph (a)(ii) above, as follows: (i) if the contact with the customer is on the telephone, the list shall be provided by U.S. mail (or by facsimile, if requested by the customer), and (ii) if the contact with the customer is a Field Contact, the list shall be provided in person during the Field Contact.

(c) In addition to complying with the requirements of Section B.10(a) and (b) above, if the contact with the customer is a Field Contact and results in a request by the customer for a list of Third Parties:

(i) A pre-printed form shall be provided to the customer. The pre-printed form shall contain the disclosures set forth in Section B.10(a) above and the Regulated Utility Activities Personnel involved in such Field Contact shall acknowledge, by checking the boxes provided for such purpose on such form, that the customer was (A) made aware of Competitive Activities products or services only upon the customer's inquiry, and (B) offered a Commission-maintained list of Third Parties.

i. One copy of the pre-printed form properly completed by the Regulated Utility Activities Personnel shall be left for the customer and one such copy shall be returned to Conectiv Power Delivery. Conectiv Power Delivery shall retain the copy of the completed form for a period of 2 years, and shall produce all copies of such completed forms for inspection upon Commission request.

(iii) Conectiv Power Delivery shall, on a quarterly basis, place a follow-up telephone call to a random sample of approximately 10% of the customers who requested a list of Third Parties during a Field Contact during the previous quarter, and inquire whether the employee complied with Section B.10(a), (b) and (c) above during the Field Contact. Conectiv Power Delivery shall retain records of such telephone calls for a period of two years, and shall produce these records for inspection upon Commission request.

(d) The list of Third Parties to be supplied to customers upon their request under Section B.10(a) above shall contain a footnote with the following statement 'This list includes the names of products and services providers who have requested to be included herein. Neither the Delaware Public Service Commission nor Conectiv Power Delivery hereby makes any recommendations nor other statements concerning the quality of the providers listed herein; nor should any such recommendations or statements be implied with respect to providers not appearing on this list.' Such list shall be compiled and maintained by the Commission and shall include any Third-Party supplier of products and services which delivers to the Commission a written request to be so included, which request shall state the product and/or service types of which such Third Party wishes to be listed as a supplier. Within a reasonable time after receipt of such written request, the Commission shall add such Third Party to the list and shall deliver such revised list to Conectiv Power Delivery. Within a reasonable period of time after receiving such revised list from the Commission, Conectiv Power Delivery shall commence supplying such revised list to customers in accordance with this provision; provided, however, that Conectiv Power Delivery shall use its best efforts to supply such revised list to customers within 15 days after receiving such revised list from the Commission.

(e) Subject to the provisions of Sections 14 and 15 below, nothing herein prohibits Delmarva personnel who are not, at the time in question, performing work for Regulated Utility Activities from specifying a preference for any Competitive Activities products or services over those of any Third Party, nor from soliciting or selling such products or services to customers, without reference to Third Parties.

11. (a) Regulated Utility Activities and Competitive Activities may jointly offer their respective products and services to the same customers (*e.g.*, joint responses to requests for proposals, trade show booths and the like) under the following conditions:

(i) Representatives of Regulated Utility Activities shall inform customers:

(A) That they work for the Regulated Utility Activities and not for the Competitive Activities; and

(B) Of the competitive nature of Competitive Activities products and services and the ability to receive Regulated Utility Services without regard to taking Competitive Activities products and services; and

(ii) The Regulated Utility Activities offerings and the Competitive Activities offerings shall be distinctly and separately priced, so that customers may select one without the other.

Notwithstanding anything above in paragraph (a) of this Section 11, Regulated Utility Activities and Affiliated Suppliers may not jointly offer Regulated Utility Services and Affiliated Supplier Services to the same customers.

(b) (i) Regulated Utility Activities Personnel shall not participate with Affiliated Suppliers in sales calls or other meetings with customers of Regulated Utility Activities, unless Regulated Utility Activities Personnel also participate with Third-Party Suppliers, on a non-discriminatory basis and on the Same Terms, in such sales calls or other meetings with customers of Regulated Utility Activities.

(ii) For a period of three years from the time the Code of Conduct is first approved by the Commission in Docket No. 99-582, Conectiv Power Delivery shall track and keep records showing each sales call or other meeting with a customer of Regulated Utility Activities in which a Regulated Utility Personnel representative participated along with either an Affiliated Supplier or a Third-Party Supplier. Such reports shall detail the date, the name and address of the customer, the identity of the Regulated Utility Activities Personnel representative attending such sales call or meeting, and the identity of the Affiliated Supplier or Third-Party Supplier attending such sales call or meeting. This reporting obligation shall cease at the end of the three-year period, unless the Commission Staff, the Department of the Public Advocate and the Company agree on the need to continue this reporting requirement beyond such period.

12. Sales Leads shall be provided by Regulated Utility Activities Personnel to Competitive Activities only upon the following conditions:

(a) The requirements of Sections B.9 and B.10(a) and (b) above shall be complied with and, in addition, if the Sales Lead is obtained during a Field Contact, the requirements of Section B.10(c) above shall be complied with;

(b) Prior to any Sales Lead being provided to Competitive Activities, an express authorization shall be obtained from the customer to do so, which authorization may be verbal or in writing; and

(c) Conectiv Power Delivery shall track and keep records of any Sales Lead provided to Competitive Activities. Conectiv Power Delivery shall retain these records for a period of 2 years, and shall produce them for inspection upon Commission request.

Notwithstanding anything above in this Section 12, Regulated Utilities Activities Personnel shall not provide Supply Sales Leads to any Competitive Affiliate.

13. Conectiv Power Delivery shall not require as a condition to providing Regulated Utility Services that a customer purchase any Competitive Activities products or services.

Provision of Services

14. Operational personnel for Regulated Utility Activities, up to and including the Vice President(s) directly responsible for Regulated Utility Activity operations, shall be different individuals from the operational personnel for Affiliated Supplier Services, up to and including the Vice President(s) directly responsible for Affiliated Supplier Services operations, and such individuals shall not be shared among Regulated Utility Activities and activities for Affiliated Supplier Services. This sharing prohibition shall not apply to officers at the Senior Vice President level and above, or to members of Boards of Directors.

15. Customer care and marketing functions, whether for Regulated Utility Activities or Competitive Activities, may be employed by a shared service company providing support services for Regulated Utility Activities and Competitive Activities; provided, however that Conectiv Power Delivery shall have a manager (below the Vice President level), for the marketing functions for Regulated Utility Activities, who is a different individual from the manager (below the Vice President level) for marketing functions for Affiliated Supplier Services; and provided, further, that Conectiv Power Delivery shall have a manager (below the Vice President level), for customer care functions for Regulated Utility Activities, who is a different individual from the manager (below the Vice President level) for customer care functions for Affiliated Supplier Services.

16. Regulated Utility Activities and Competitive Activities shall be permitted to share office space, office equipment, services and systems, and each can access the computer or information systems of the other, so long as adequate security and system protections are in place to prevent the accessing of information or data of Regulated Utility Activities by Competitive Activities that would be in violation of other provisions of this Code of Conduct. Each of the Commission Staff and the Department of the Public Advocate shall have the opportunity to review such security and system protections periodically upon its request, at times to be mutually agreed upon by such requesting party and the Company.

Accounting for Costs

17. Transactions between Regulated Utility Activities and Competitive Activities shall be accounted for in accordance with the then-current Cost Accounting Manual in effect for Conectiv Power Delivery.

C. *Incorporation by Reference of Other Rules Governing Conduct*

Conectiv Power Delivery hereby adopts as a part of the Code of Conduct, and incorporates herein by reference, the 'Standards of Conduct of Delmarva,' Corporate Policy No. 8109, effective January 3, 1997, which were adopted by Conectiv Power Delivery in compliance with FERC regulations at 18 C.F.R. § 37.4 *et seq.*, as such Standards of Conduct may be modified, amended or superseded from time to time (the 'Standards of Conduct'); provided that, to the extent that there is a conflict between (a) any provision in the Standards of Conduct covering a specific aspect of the Regulated Utility Activities and/or Competitive Activities and (b) any provision in the Code of Conduct; then such specific provision in the Standards of Conduct shall govern.

D. *Procedure for Modification of Code of Conduct*

The Code of Conduct shall be modified in accordance with the following procedure:

1. Conectiv Power Delivery shall file an application with the Commission requesting approval for the proposed modification(s) and setting forth the reasons therefor.

2. Pursuant to established Commission procedures for changes to regulations governing regulated utilities, the Commission shall approve, deny or modify the application, in whole or in part, within 60 days after the filing of the application; provided that the Commission, in its discretion, may set a longer time period for the taking of such action and may set the matter for hearing before a Hearing Examiner.

E. *Dispute Resolution/Compliance with Code of Conduct*

Disputes concerning Conectiv Power Delivery's compliance with the Code of Conduct shall be resolved in accordance with the following procedures:

1. Any Third Party alleging that Conectiv Power Delivery has failed to comply with the Code of Conduct and wishing to have independent resolution thereof shall file a formal complaint with the Commission which meets the requirements of Section 8(b) of the Department of Administrative Services, Public Service Commission Rules of Practice, within 45 days after discovery of such alleged failure.

2. Proceedings on such complaint shall be held in accordance with the Department of Administrative Services, Public Service Commission Rules of Practice.

F. *Reporting Requirements*

1. Conectiv Power Delivery shall report to the Commission, on an annual basis:

(a) All affiliated companies;

(b) All contracts entered into with affiliated companies, and all of the types of transactions undertaken with affiliates without a written contract;

(c) The dollar amount charged with respect to affiliate transactions, by affiliate by account charged;

(d) The basis used to record affiliate transactions charges (*i.e.*, book value, fair market value, fully-distributed cost);

a. Total costs allocated or charged, to or from, Conectiv Power Delivery, by each other Conectiv line of business (*e.g.*, Conectiv Energy Wholesale, Conectiv Energy Retail, Conectiv Communications, Conectiv Services, Conectiv Solutions, and Concctiv Thermal Systems), and the allocation of infrastructure (*e.g.*, shared services costs from Conectiv Resource Partners, Inc.) costs to each line of business; and

(f) Updates of the allocation factors used for each infrastructure cost center.

2. In addition, Conectiv Power Delivery shall:

(a) Make available the books and records of Conectiv, the parent company, and other affiliates when required in the application of Conectiv Power Delivery's Code of Conduct and Cost Accounting Manual;

(b) Maintain books of account and supporting records in sufficient detail to permit verification of compliance with Conectiv Power Delivery's Code of Conduct and Cost Accounting Manual;

(c) Continue to submit all reports that are currently filed with the Commission;

(d) Notify the Commission of any plans to pledge Regulated Utility Activities revenues or assets in excess of $10 million; and

(e) For a period of two years from the time this Code of Conduct is first approved by the Commission in Docket No. 99-582, file semi-annual reports showing transfers of employees made: (a) from Conectiv Power Delivery to Competitive Activities; (b) from Competitive Activities to Conectiv Power Delivery; (c) from Conectiv Resource Partners, Inc. to Competitive Activities; and (d) from Competitive Activities to Conectiv Resource Partners, Inc. These reporting obligations shall cease at the end of the two-year period, unless the Commission Staff, the Department of the Public Advocate and the Company agree on the need to continue this reporting requirement beyond such period; provided that,

if the parties cannot agree and any of such parties believes the reporting obligations should continue, such party may submit the issue to the Commission for resolution.

End of Document

TAB 7

West's Delaware Code Annotated
Title 26. Public Utilities
Chapter 1. Public Service Commission
Subchapter V. Hearings and Appeals

26 Del.C. § 512

§ 512. Settlements are to be encouraged

Currentness

(a) Insofar as practicable, the Commission shall encourage the resolution of matters brought before it through the use of stipulations and settlements.

(b) The Commission's staff may be an active participant in the resolution of such matters.

(c) The Commission may upon hearing approve the resolution of matters brought before it by stipulations or settlements whether or not such stipulations or settlements are agreed to or approved by all parties where the Commission finds such resolutions to be in the public interest.

Credits
70 Laws 1995, ch. 48, § 8, eff. June 12, 1995.

26 Del.C. § 512, DE ST TI 26 § 512
Current through 80 Laws 2016, ch. 430. Revisions to 2016 Acts by the Delaware Code Revisors were unavailable at the time of publication.

End of Document

TAB 8

West's Delaware Code Annotated
Title 29. State Government
Part VIII. Departments of Government
Chapter 87. Department of State
Subchapter I. General Provisions

29 Del.C. § 8716

§ 8716. Division of the Public Advocate

Effective: July 24, 2013
Currentness

(a) There is established within the Department of State the Division of the Public Advocate. The Public Advocate shall be a person qualified by training and/or experience to perform the duties of the office. Beginning in the 149th General Assembly, the Public Advocate shall be appointed by the Governor with the advice and consent of the majority of the Senate to serve a term of 4 years at the pleasure of the Governor. The Public Advocate shall be a full-time employee of the State.

(b) No person shall be eligible for appointment to be Public Advocate who owns or controls, in that person's own name or as a fiduciary, or whose spouse or minor child residing in that person's household owns or controls any stock, note or debenture in any public utility, or who holds any office or position with any public utility or whose employment or vocation depends directly upon or is under the control of a public utility.

(c) In the event of death, resignation, temporary incapacity or removal of the Public Advocate and prior to the appointment of a successor, the Governor may appoint an Acting Public Advocate. The Acting Public Advocate shall have all the powers and shall perform all the duties and functions of the Public Advocate during such absence or incapacity or until a successor is duly qualified and appointed.

(d) The Public Advocate shall comply with and be held strictly accountable for compliance with the highest standards of Chapter 58 of this title and § 22, Article II of the Delaware Constitution. The Division of the Public Advocate is an agency subject to Chapters 64 and 100 of this title.

(e) The Public Advocate shall have the following powers and duties:

(1) To appear before the Public Service Commission on behalf of the interest of consumers in any matter or proceeding over which the Commission has jurisdiction and in which the Public Advocate deems the interest of consumers requires such participation.

(2) To advocate the lowest reasonable rates for consumers consistent with the maintenance of adequate utility service and consistent with an equitable distribution of rates among all classes of consumers; provided, however that the Public Advocate shall principally advocate on behalf of residential and small commercial consumers and shall not be required to advocate for any class of commercial or industrial consumers that the Public Advocate determines in his or her sole discretion on a case by case basis has the ability to advocate on its own behalf before the Public Service Commission.

(3) To appear on behalf of the interest of consumers in the courts of this State, the federal courts and federal administrative and regulatory agencies and commissions in matters involving rates, service and practices of public utilities.

(4) To hire, from time to time, as needed, in connection with proceedings before the Commission, experts in the utility regulation field, including, but not limited to, economists, cost of capital experts, rate design experts, accountants, engineers and other specialists. A budget for compensation and/or expenses of these experts shall be provided annually through the Delaware Public Utility Regulatory Revolving Fund. Nothing in this section shall be construed to preclude the Public Advocate from applying to the General Assembly for additional funds in specific instances, including emergencies, and from receiving such additional amounts as the General Assembly shall determine.

(5) To have the same access to and the same right to inspect any and all books, accounts, records, memoranda, property, plant facilities and equipment of the public utilities as is afforded by law or by rule of the Public Service Commission to any other party in interest.

(6) To have full access to the records of the Public Service Commission.

(7) To call upon the assistance of the staff and experts of the Public Service Commission in the performance of duties.

(8) To appoint, fix the compensations and terms of service and prescribe the duties and powers of such staff as may be necessary for the proper conduct of the work of the Division of the Public Advocate, within the conditions and limitations imposed by the merit system of personnel administration.

(9) Upon request of the Governor, the Secretary of the Department, or the General Assembly, the Public Advocate shall provide guidance on matters relating to energy policy and utility consumers, and shall consider such other matters as may be referred to the Public Advocate or the Division by the Governor, the Secretary of the Department, or the General Assembly. The Public Advocate may study, research, plan and make advisory recommendations to the Governor, the Secretary of the Department, or the General Assembly on matters it deems appropriate to advocate on behalf of public utility consumers.

(f) The Public Service Commission shall notify the Public Advocate of all hearings and meetings of the Commission and shall forward to the Public Advocate copies of all applications submitted by public utilities and all formal complaints and petitions filed with the Commission. No formal action taken by the Commission without proof of the receipt of notice by the Public Advocate shall have any legal effect.

(g) The Public Advocate shall be entitled to be present and be heard at any public meeting of the Public Service Commission.

(h) When the Public Advocate shall determine to intervene in a matter before the Public Service Commission, the Public Advocate shall file a statement to that effect with the Public Service Commission. Thereupon, the Public Advocate shall

be deemed a party in interest and shall have full power to present evidence, subpoena and cross-examine witnesses, submit proof, file briefs, appeal and do any other act appropriate for a party to the Commission.

(i) The Public Advocate shall make an annual report to the Governor and the General Assembly of the Division's activities, and shall render such other reports as the Governor or General Assembly may from time to time request or as may be required by law.

Credits

71 Laws 1997, ch. 138, § 17; 70 Laws 1995, ch. 186, § 1, eff. July 10, 1995. Redesignated from 29 Del.C. § 8808 and amended by 75 Laws 2005, ch. 88, §§ 7, 17(3), eff. July 1, 2005. Amended by 79 Laws 2013, ch. 139, § 1, eff. July 24, 2013.

Codifications: 29 Del.C. 1974, § 8808

29 Del.C. § 8716, DE ST TI 29 § 8716

Current through 80 Laws 2016, ch. 430. Revisions to 2016 Acts by the Delaware Code Revisors were unavailable at the time of publication.

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF DELAWARE

IN THE MATTER OF THE APPLICATION OF DELMARVA POWER & LIGHT COMPANY FOR AN INCREASE IN ELECTRIC BASE RATES AND MISCELLANEOUS TARIFF CHANGES (Filed May 17, 2016)	)))))	PSC DOCKET NO. 16-0649

CERTIFICATE OF SERVICE

I hereby certify that on February 27, 2017, I caused a copy of both the public and confidential versions of **DELMARVA POWER & LIGHT COMPANY'S MOTION TO CONVERT EVIDENTIARY HEARING** in this docket to be filed in Delafile with a courtesy copy provided to counsel for the Commission Staff, the Public Advocate and the Delaware Energy Users Group via electronic mail.

/s/ *Pamela J. Scott*
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Dated: February 27, 2017